

From the Bubble Act to the pre-incorporation trust: investor protection in Quebec law

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Résumé de l'article

La possibilité de lier une compagnie qui n'existe pas par un contrat conclu en son nom avant sa date d'incorporation reste un des problèmes les plus difficiles du droit corporatif contemporain. Au Québec, la question des contrats pré-incorporatifs est en partie traitée à l'article 29 de la *Loi des compagnies S.R.* 1964 c. 271, qui permet la création d'un fidéicommiss en vue d'une constitution en corporation.

L'origine de l'article 29 reste énigmatique : l'historique de cette disposition nous renvoie à l'étude du phénomène des compagnies non-incorporées au Québec et d'une manière plus générale, à l'examen du *Bubble Act*, première loi des temps modernes à réglementer, pour la protection de l'épargne, les activités des compagnies à but lucratif.

L'introduction historique permet de placer l'article 29 dans sa véritable perspective et nous amène à considérer le fidéicommiss pré-incorporatif dans ses applications particulières. Aussi, la jurisprudence et la doctrine ont établi des règles précises concernant l'interprétation, la création et l'effet de ce fidéicommiss statutaire et ces divers points sont examinés en détail. Enfin, la discussion aborde le sujet des devoirs des promoteurs à l'égard de la future compagnie et des tiers investisseurs.

Le fidéicommiss pré-incorporatif permet donc d'observer, dans un panorama historique qui couvre près de trois siècles, le souci constant des législateurs et des tribunaux de protéger l'investissement contre la cupidité des spéculateurs et fait ressortir, dans les législations contemporaines en la matière, la pérennité des problèmes soulevés et des solutions retenues.

From the Bubble Act to the pre-incorporation trust: investor protection in Quebec law*

Robert DEMERS**

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The historical spoor of the corporation indeed leads into the past but unfortunately goes nowhere in particular but rather everywhere in general.

G. F. McGuigan, "The emergence of the unincorporated company in Canada," (1964) 2 *U.B.C. Law R.* 31, at pp. 32-33.

The problem of adequate protection of the investing public is probably as old as company law itself. The *Bubble Act*¹ was the first statute of modern times that made any serious attempt to regulate the securities market for the benefit of investors². As will be shown, this enigmatic piece of legislation had considerable impact not only on the general complexion of modern company law but also influenced the evolution of commercial law even in the British colonies.

Thus, in Lower-Canada, the *Bubble Act* made a timid appearance and brought about the formation of unincorporated companies, a rather singular anomaly in a civil law jurisdiction. Moreover, in Quebec law, much of the discussion on promoters and their duties is somewhat related to this historical enquiry. For this reason, it was considered useful to examine many of the controverted issues surrounding the historical aspects of Quebec law on company promotion before embarking upon a detailed analysis of promoters' rights and duties in that jurisdiction.

This approach affords an interesting vista on the peculiarities of Quebec law in this field: the simultaneous application of the Civil Code, the *Companies Act*³ and the *Securities Act*⁴ to company promotions in Quebec will indicate clearly enough the unique position resulting from such interaction.

I. The *Bubble Act* and its implications

A. THE *Bubble Act* IN ENGLAND

1. *The rise and fall of the South Sea Company*

Up to the beginning of the eighteenth century, English companies were usually royal enterprises⁵ and participation in the management and capital of such corporations was limited to a privileged few⁶. However,

1. (1720) 6 Geo. I c. 18 (U.K.).

2. L.C.B. GOWER, *The principles of modern company law*, 3rd ed, Stevens and Sons, London, 1969, at p. 30.

3. R.S.Q. 1964 c. 271. (Hereinafter referred to as the *Companies Act*.)

4. R.S.Q. 1964 c. 274. (Hereinafter referred to as the *Securities Act*.)

5. W. R. SCOTT, *The constitution and finance of English, Scottish and Irish joint-stock companies to 1720*, vol. I, Cambridge University Press, Cambridge, 1912, at p. 341; C. A. COOKE, *Corporation, trust and company*, Manchester University Press, Manchester, 1950, at pp. 49-52, 60 and 61. In the earlier part of the seventeenth century, new corporations were viewed as a threat to "the Common Wealth": Sir E. COKE, *The second part of the Institutes*, 3rd ed., Crooke & Co., London, 1669, at p. 540.

6. GOWER, *op. cit.*, at pp. 24-25; COOKE, *op. cit.*, at pp. 57-58.

the commercial evolution of the country favoured the multiplication of private companies: division of share capital into relatively small fractions gave the ordinary *bourgeois* an opportunity of sharing in the prosperity of the land⁷, and private companies became a common feature of the period. The creation of capital also called for its circulation and it was at that same time that stockbrokers made their appearance in the coffee-houses of London⁸.

In this climate of economic prosperity the South Sea Company was founded in 1711⁹. It is important to note that its main promoter, Lord Harley, was at the time Chancellor of the Exchequer¹⁰, and that the participation of the government in the affairs of this company was to be so active that King George I himself became governor in the elections of 1718¹¹. This was no mere coincidence: the national debt, in 1711, reached millions of pounds and Harley somehow hoped to rid the nation of this burden with his new company¹². His plan was a clever one: government bonds, which formed the bulk of the national debt, became redeemable in exchange for shares in the South Sea Company¹³.

The formula was very popular: holders of government securities were more than happy to exchange them for shares the value of which was rising steadily because of intense speculation. But this success was short lived: the Company's main asset was the national debt and although the quotation of shares was to reach incredible heights¹⁴, this bore no relation to the Company's true value. Speculation became hysterical: the government's approval of the South Sea scheme had the adverse effect of

7. SCOTT, *op. cit.*, at p. 341. Before 1700, the value of a single share was so considerable that ordinary persons had to associate in order to buy one. Thus, in the *New River Company*, one share was worth £258. *Vide* Scott, *ibid.*, at p. 155.

8. For an interesting and humorous history of that period, *vide* A. JENKINS, *The Stock Exchange Story*, Heinemann, London, 1973, at pp. 16-39; E. V. MORGAN and W. A. THOMAS, *The Stock Exchange*, Elek Books, London, 1969, at pp. 11-42.

9. GOWER, *op. cit.*, at p. 28, n. 28.

10. JENKINS, *op. cit.*, at p. 27.

11. J. CARSWELL, *The South Sea Bubble*, The Cresset Press, London, 1960, at p. 73. Even the royal mistresses had their share of the benefits that were to come out of this national enterprise: on this last point, *vide* L. O. PIKE, *A history of crime in England*, vol. 2, Smith, Elder & Co., London, 1873-76, at p. 303. The official parliamentary enquiry that was to investigate into the affairs of the Company after 1720 showed the incredible degree of official corruption that marked this whole era: Pike, *op. cit.*, at pp. 303-304. *Vide* also Cooke, *op. cit.*, at p. 82.

12. JENKINS, *op. cit.*, at pp. 27-28.

13. CARSWELL, *op. cit.*, at pp. 35 and 54; Cooke, *op. cit.*, at pp. 82-83.

14. In June 1720, the shares were quoted at 1000 but fell in the same year to 124 in December: Jenkins, *op. cit.*, at p. 32.

encouraging the creation of all types of companies that were formed for the sole purpose of creating a market for their shares¹⁵. The passion for gaming in stocks that possessed the London market was finally calmed by the proclamation of the *Bubble Act*¹⁶.

The exact effect of that statute to this day remains somewhat of a mystery¹⁷: it declared illegal certain undertakings that acted as corporate bodies and raised a transferable stock without authority of a royal charter or Act of Parliament and outlawed undertakings acting under obsolete charters¹⁸. However, it exempted from these prohibitions companies formed before 1718¹⁹ and all partnerships²⁰.

The *Bubble Act* was in no way intended as a sanction against the South Sea Company: on the contrary, some authorities suggest that it was enacted to eliminate competition in favour of that body²¹. The public, however, lost confidence: shares dropped in value dramatically and investors lost considerable fortunes. A Parliamentary enquiry revealed the extent of official corruption that finally caused the collapse of the Company²², but other scapegoats had to be found to satisfy the public's need for culprits. Attention was directed to "the pernicious art of Stock-jobbing"²³, that had appeared recently on the London market, but this was not a satisfying victim. The public became somehow convinced that responsibility for the whole collapse lay not with the government or the brokers but with the numerous joint-stock companies formed during the last decade. Companies became an "object of suspicion and attack"²⁴ and this popular feeling was to have important repercussions on the future of company law in England.

24. C. T. CARR, *The general principles of the law of corporations*, Cambridge University Press, Cambridge, 1905, at pp. 107-108.

15. GOWER, *op. cit.*, at p. 28.

16. GOWER, *op. cit.*, at pp. 28-30.

17. GOWER, *op. cit.*, at p. 29: "Exactly what it did is, however, somewhat obscure . . ."

18. (1720) 6 Geo. I c. 18, s. 18.

19. *Ibid.*

20. *Ibid.*

21. CARSWELL, *op. cit.*, at p. 139; COOKE, *op. cit.*, at pp. 83-84.

22. SCOTT, *op. cit.*, at p. 437.

23. JENKINS, *op. cit.*, at p. 20, referring to a report of the *Parliamentary Commission on Trade in England* (1696). Some attempt was made to blame the whole scandal on brokers: CARSWELL, *op. cit.*, at p. 16. Brokers had been viewed with great suspicion since their appearance in Change Alley and "it would not be a serious exaggeration to say that after the revolution the stockbroker gradually replaced the jesuit as everyman's idea of a conspirator . . ." CARSWELL, *ibid.*

2. *Unincorporated joint-stock companies*

Most commentators agree that the main effect of the *Bubble Act* was to restrain for more than a century the incorporation of commercial enterprises: after the great Bubble, companies remained unpopular in the public eye and, as a general rule, the Crown refused to grant charters to promoters of such associations²⁵. Business however continued: some corporate form was necessary to allow for the association of individuals and the creation of capital, and this is where the unincorporated joint-stock company reappeared on the commercial scene. Such bodies had always existed, but after 1720 they became extremely popular²⁶.

The companies were formed, like partnerships, by a contract²⁷ whereby the parties agreed to be united in an undertaking with a fixed capital, divided into transferable shares²⁸. Unlike a partnership, however, the real and personal property of the company was transferred to a trustee²⁹ or a group of trustees³⁰: this particular feature allowed the trustee to act without having to assemble all of the shareholders³¹. The trustee was the only person who had a sufficient interest to bring actions at law for the protection of the property held by him³² but this right of action had

25. A. B. DU BOIS, *The English business company after the Bubble Act 1720-1800*, The Commonwealth Fund, New York, 1938, at pp. 1-41; GOWER, *op. cit.*, at p. 32; R. R. PENNINGTON, *Company Law*, 3rd ed., Butterworths, London, 1973, at p. 8; COOKE, *op. cit.*, at pp. 80 and 186; W. S. HOLDSWORTH, *The early history of commercial societies* (1916) 28 *Juridical R.* 305, at pp. 340-344.
26. SCOTT, *op. cit.*, at pp. 246-247, shows that such companies had existed before the South Sea Bubble. See also: G. F. MCGUIGAN, *The emergence of the unincorporated company in Canada* (1964) 2 U.B.C. Law R. 31 at p. 37.
27. DU BOIS, *op. cit.*, at p. 217; the members signed a deed of settlement containing the conditions of their contract. *Vide* also J. SMITH et Y. RENAUD, *Droit québécois des corporations commerciales*, vol. 1, Judico Inc., Montréal, 1974, at p. 11.
28. GOWER, *op. cit.*, at p. 33.
29. DU BOIS, *op. cit.*, at p. 217; COOKE, *op. cit.*, at pp. 86-87. The trustee ordinarily acted on the instructions of the members, when questions arose concerning this property: GOWER, *op. cit.*, at p. 34.
30. L. S. SEALY, *Equitable obligations in the management and promotion of companies*, Yorke Prize Essay, Cambridge, 1959, at pp. 39-40, 42 n. 25.
31. *Supra* n. 29. It is interesting to note that this same argument is used in Quebec law to justify the existence of a trustee under the *Special Corporate Powers Act* R.S.Q. 1964, c. 275. The trustee for bondholders under a trust deed made in pursuance of that statute can sue at law for any question arising out of the deed to the exclusion of the bondholders. This is predicated on questions of convenience: *Cité de Trois-Rivières v. The Sun Trust Co.* (1923) 34 Que. K.B. 351, at pp. 353, 357 and 364.
32. DU BOIS, *op. cit.*, at p. 218.

definite limits³³. In certain cases, the trustee was also responsible for the transfer of shares in the company³⁴.

Thus, the unincorporated company centered on the trustee: in the eighteenth century, he was a common feature of the commercial life³⁵ and the unincorporated company is a good illustration of his omnipresence. Considerable research has been carried out on the legal aspects of such companies³⁶ and it is beyond the scope of our enquiry to discuss this: however, it is the more striking features of unincorporated bodies that should be underlined.

The presence of a trustee and a transferable stock³⁷ indicates a major difference between such companies and partnerships and highlights the thin line that divided them from the despised chartered corporations³⁸. The *Bubble Act* in England thus had a double effect. It prevented the massive incorporation of companies for private purposes and encouraged the creation of unincorporated bodies. This was to change the traditional forms of corporate activity and had a lasting impact on English law. Even to this day, the law reports contain the odd references to that disastrous era³⁹.

33. The only rights of action that the trustee had were those relating to the property of the company that was vested in him: for any other question involving the company, the whole body had to be called in although the courts of equity tried to relax this difficult requirement: *Du Bois, op. cit.*, at pp. 220-221. In a sense, this is the rule of *Foss v. Harbottle* (1843) 2 Hare 461 as applied to unincorporated companies.

34. *Du Bois, op. cit.*, at p. 222.

35. *Ibid.*

36. *Du Bois, op. cit.*, chapter 3.

37. *Du Bois, op. cit.*, at pp. 233-235, 237 and 239 for more details on the trustee; pp. 222, 232, 238-241, 359-360 for more details on the transferable shares.

38. R. R. Formoy, *The historical foundations of modern company law*, Sweet and Maxwell, London, 1923, at pp. 38 and following.

39. See, e.g., Lord Cross' speech in *Ebrahimi v. Westbourne Galleries Ltd.* [1973] A.C. 360, at p. 383. Note that a similar sequence of events happened in France at the same period: this was Law's famous Mississippi scheme that brought ruin to the whole of the Kingdom. See J. Escarra et J. Rault, *Traité théorique et pratique de droit commercial*, vol. 1, Recueil Sirey, Paris, 1950, at pp. 19 and following, for a historical study of this question. See also: *Green v. Charterhouse Group Canada Ltd.* [1973] 2 O.R. 677, at p. 709. The prohibition under the new federal act of paying for shares with promissory notes [*Canada Business Corporations Act* S.C. 1974-75-76 c. 33, s. 25 (5)] might be a statutory safeguard against future bubble companies: as seen above, the South Sea Co. was financed in major part by the national debt (*supra* n. 13) with the curious result that the company's main asset was in fact a liability of millions of pounds. The federal legislature clearly indicated in s. 25 of the new Act the danger of such methods of finance by refusing to allow the creation of corporate capital with liabilities, private or national.

Whether the *Bubble Act* had any repercussions in Quebec is the question that will now be examined: at the outset, it might be observed that a jurisdiction of civil law could adapt only with great difficulty to this type of legislation and that the reception of such a statute in Quebec could possibly result in some legal anomaly.

B. THE *Bubble Act* IN LOWER-CANADA

In 1763, more than forty years after the *Bubble Act*, the French colony of *Nouvelle-France* was ceded to the English by the Treaty of Paris. This had important consequences from the point of view of company law: the granting of letters-patent to corporations became a matter of discretion for the representatives of the English King and, surely, the views of the colony's administrators were not much different in this respect from those of the Attorney-General in England. Whether or not the *Bubble Act* was applicable in the new colony will now be examined and the subsidiary question of knowing whether unincorporated companies appeared in the province will also be discussed.

1. *The Bubble Act in Quebec*

The state of the laws in the new English colony after 1763 was so confused that it has been described as "a sort of noisy chaos" by one commentator⁴⁰. To determine whether or not a particular English statute applied thus becomes a difficult exercise and the *Bubble Act* is no exception to this rule.

Did the Treaty of Paris have the effect of introducing to the colony English law and, more particularly, the *Bubble Act*?

When a foreign colony is conquered or ceded, constitutional law indicates that the laws in force in that colony remain valid until they are repealed by the Crown. Thus, Blackstone writes:

"But in conquered or ceded countries, that have already laws of their own, the King may indeed alter and change those laws; but, till he does actually change them, the ancient laws of the country remain . . . Our American plantations are principally of this latter sort, being obtained in the last century either by right of

40. H. M. Neatby, *The administration of justice under the Quebec Act*, University of Minnesota Press, Minneapolis, 1937, at p. 3. The author also quotes Chief Justice Smith who considered the law of that period as some kind of "comedy of errors": *ibid.*, at p. 228. *Vide* also pp. 154-155.

conquest and driving out the natives . . . or by treaties. And therefore the common law of England, as such, has no allowance or authority there . . ."⁴¹

By the *Act of Quebec*⁴², the Crown did not alter the common law of the Province⁴³ but only modified the criminal law by replacing it with the principles of English law⁴⁴. Commercial law, except for a few minor modifications, was to remain substantially the same as under the French *régime*⁴⁵ : as a consequence, one can conclude on matters of principle that the Crown did not intend to extend to the colony the application of the *Bubble Act*. Even in the eighteenth century, legal opinion favoured the view that the statute was only of local application and did not encompass the whole of the Empire⁴⁶.

The jurisprudence of our Province confirms this opinion. In an early case that has never been cited on this issue, *White & al. v. The Ship Daedalus*⁴⁷, the Court examined the point and set out the reasons why, in its opinion, the *Bubble Act* could not apply to the colony⁴⁸. Sir William

41. *Commentaries on the laws of England*, vol. 1, 15th ed., Cadell & Davies, London, 1809, at pp. 107-108. This principle is still admitted today: O. Hood PHILLIPS, *Constitutional and administrative law*, 5th ed., Sweet & Maxwell, London, 1973, at pp. 590-591.

42. (1774) 14 Geo. III c. 83 (U.K.).

43. *Ibid.*, article 8.

44. *Ibid.*, article 11; NEATBY, *op. cit.*, at pp. 298 and following. Note however that only the criminal law of general application extended to the colony and not offences that were of a purely local nature in England: *Isaac Rousse, Ex parte* (1828) Stu. R. 321 (K.B.).

45. NEATBY, *op. cit.*, at pp. 44, 50, 54, 208 and 212. "Not one change of the slightest importance was made in substantive commercial law throughout the entire period": *ibid.*, at p. 54.

46. DU BOIS, *op. cit.*, at p. 25 and p. 66, n. 139; Labrie and Palmer, "The Pre-Confederation History of Corporations in Canada", in *Studies in Canadian company law*, vol. 1, Butterworths, Toronto, 1967, (J. S. Ziegel, ed.), at p. 37. Cf. *Bank of Upper Canada v. Bethune* (1835) 4 U.C.Q.B. (o.s.) 165 and 193 where Robinson, C. J., was of the opinion that the simple Cession of the Colony to the English operated the extension of the *Bubble Act* to Canada. As established previously, this is contrary to the principles of constitutional law. *Vide supra* n. 41.

47. *Stuart's Reports* 130. Judgment was rendered on the 11 December 1818 by Sir William Scott in the High Court of Admiralty (Division of Quebec). The case is a remarkable one for the period.

48. This case deals with the first part of the *Bubble Act*: in articles 1-17 of the Act, regulations were set out to control maritime insurance (bottomry) and to create a monopoly in favour of the London and Royal Exchange Assurance Co. On this point: GOWER, *op. cit.*, at p. 29, n. 31; COOKE, *op. cit.*, at p. 121. In the *White* case, two merchants of Quebec had loaned money on a bottomry bond and were claiming payment from the ship's owner. The debtor refused to pay pleading that such a loan was contrary to the *Bubble Act* and the special privileges created in favour of the London Insurance Companies. Sir W. SCOTT pointed out that those privileges ". . . no doubt,

Scott rendered judgment: he put forward two reasons why he refused to apply the statute. His first argument was one of policy: the *Bubble Act* was "a statute for restraining certain unwarrantable extravagancies, projects and schemes, or as they were called in the language of the times, bubbles, and for protecting owners of ships from exorbitant and fraudulent insurances . . ." ⁴⁹. The statute was enacted to correct multiple frauds brought about by the abuses of bubble companies—but such a situation never arose in Canada. For this reason, the learned judge concluded:

" . . . it is perfectly clear that such an act could not apply to America. There were no existing circumstances at that time to render it necessary to erect such corporations in that part of the world . . . if then, its policy did not extend to America, so neither did its prohibitions . . ." ⁵⁰.

Any other conclusion would be harmful to the economy of the colony where "capital in surely infinitely more scarce . . . than in Great Britain . . ." ^{50a}.

His Lordship's other argument was more technical: if truly the *Bubble Act* was applicable to all the colonies, why was it necessary to extend its application by specific legislation in 1741 to the New England colonies⁵¹? A possible inference is that the Imperial Parliament itself considered it inapplicable to such dominions without clear extension thereto. The court then came to the conclusion that the statute did not apply in Quebec, a position that conforms to the constitutional principles examined above⁵².

Notwithstanding, some commentators argue that if the *Bubble Act* was not extended in its application to Quebec by the simple Cession of 1763, then it must have been by the Act of 1741⁵⁴. However, when one examines the statute more closely, it becomes apparent that it was in-

in England, had full and entire operation . . ." (*supra* n. 47, at p. 131), and then went on to consider whether or not the *Bubble Act* applied to Canada. His conclusions, however, are of a more general nature and deal with the application of the whole statute, which includes article 18, regulating the existence of bubble companies. For bottomry bonds in civil law, *vide* articles 2693-2711 C.c.

49. *Supra* n. 47, at p. 131.

50. *Ibid.*, at p. 132.

50a *Ibid.*

51. His Lordship refers to the Act (1741) 14 Geo. II c. 37: *ibid.*, at p. 132. This statute is examined *infra*.

52. *Ibid.*, at p. 132; *supra* n. 41.

53. "An act for restraining and preventing several unwarrantable schemes and undertakings in His Majesty's Colonies and Plantations in America."

54. R. C. B. Risk, *The nineteenth century foundations of the business corporation in Ontario* (1973) 23 U. of T.L.J. 270, at p. 300, n. 175; Labrie and Palmer, *op. cit.*, at p. 37.

tended, in its application, for the New England Colonies only and not for the whole empire, as is commonly assumed⁵⁵. In 1740, promoters in Massachusetts were desirous of founding specialized banks: some doubt arose as to the validity of such schemes in view of the *Bubble Act* and the question was submitted to the Attorney-General of England for his opinion. He saw no objections to these undertakings, adopting the view that the statute did not apply to the colonies⁵⁶. A petition was then presented to Parliament to extend the application of the *Bubble Act* to the New England Colonies⁵⁷ and the Act 14 Geo. II c. 37 was adopted. The formulation of the statute indicates clearly that it was meant for that particular region of North America only⁵⁸; this is even more apparent when one considers that in 1741 Quebec was still a French colony and was to remain one for nearly a quarter of a century.

Consequently, unless the statute was made applicable to Quebec after the Cession⁵⁹, it could not have brought about the application of the *Bubble Act*.

In concluding, it is difficult to assert with complete certainty that the statute was not law in the province⁶⁰ but when one considers the very

55. Smith et Renaud, *op. cit.*, vol. I, at p. 11.

56. *Vide supra* n. 46.

57. Du Bois, *op. cit.*, p. 66, n. 141.

58. Sir W. HOLDSWORTH, *A history of English Law*, vol. II, Methuen & Co. Ltd, London, 1937, at p. 88.

59. *Vide supra* n. 41.

60. This difficult question becomes even more complicated when one considers that some authorities argue that the *Bubble Act* might have been imported into the Province at the same time as criminal law. The *Act of Quebec* replaced the French penal laws with English criminal law: *supra* n. 44. The question thus becomes: was the *Bubble Act* part of English criminal law at the time? Most authorities agree that the offence established by the Act was a public nuisance: the statute itself admits this (art. 18). Public nuisances in English law are part of the criminal law: commentators list amongst such offences the one created by the statute. On these points see: BLACKSTONE, *op. cit.*, vol. III, at p. 216; vol. IV, at pp. 166-167; C. VINER, *A general abridgement of law and equity*, vol. 16, 2nd ed., G.G.J. and J. Robinson, London, 1792, at pp. 21-22; M. BACON, *A new abridgement of the law*, vol. 5, 7th ed., A. Straban, London, 1832, at pp. 794-95, 798; *Rex v. Caywood* 1 Stra. 472; 93 E.R. 641 (for what seems to be the only criminal prosecution reported under the Act); L.C.B. GOWER, *A South Sea heresy?* (1952) 68 L.Q.R. 214, at p. 220, n. 48.

Blackstone describes contraventions to the statute as "heinous offences": *op. cit.*, vol. IV, at pp. 115-117, where the author also gives details on the punishment imposed on offenders, *praemunire*.

When English criminal law became part of Quebec law did this have the effect of introducing the *Bubble Act* to the province? In *Bank of Upper Canada v. Bethune*, *supra* n. 46, Robinson, C.J., suggests that this was possible but mentions this merely in *obiter: ibid.*, at p. 171. *Vide also* J. CRÉMAZIE, *Les lois criminelles anglaises*

local nature of the legislation, the state of the Canadian economy at the period and the willingness of the English administration to leave intact the legal heritage of the colony, one can seriously doubt the view that admits the application of the statute to Quebec.

2. *Unincorporated joint-stock companies in Quebec*

As a rule, in England, after the South Sea Bubble, royal charters were not granted to commercial enterprises because of the unpopularity of such bodies: this, as established previously, was the main reason for the appearance of the unincorporated company as an adequate substitute⁶¹. In Canada, the *Bubble Act* probably did not apply. As a logical consequence, charters should have been granted for commercial purposes and, in principle, unincorporated companies should have been unknown in the law of the Province. This, however, was not so: the British administration probably followed closely the Home government's policy in this matter and, as a rule, refused to grant letters-patent for commercial purposes⁶². This as a consequence would explain the appearance of unincorporated bodies in Quebec after the Cession. This point will now be examined. Article 1889 of the Quebec Civil Code reads as follows:

"1889. Joint-stock companies are formed either under the authority of a royal charter, or of an act of the legislature, and are governed by its provisions; or they are formed *without such authority*, and in the latter case, are subject to the same general rules as partnerships under a collective name"⁶³.

It is indeed surprising to find in the Civil Code a distinction established between incorporated and unincorporated companies. However,

traduites et compilées de Blackstone, Chitty . . . et telles que suivies en Canada, Fréchette et Cie., Québec, 1842, at p. 63. This view however is a simplistic one. The whole of the English criminal law was not made applicable to the colony because some crimes were of a purely local nature in England: only the general principles of criminal law were adopted in the colony and the Quebec Court of Appeal admitted this point as early as 1828: *Isaac Rousse, Ex parte* (1828) Stu. R. 321 (K.B.). One can argue on this issue that the offence created by the *Bubble Act* was only to apply locally to England because it is only there that the problems arose. There were no similar frauds in Canada at the time, and as pointed out by Sir W. Scott in the *White* case, *supra* n. 47, if the policy of the statute did not apply to Canada, then the only conclusion is that neither did its prohibitions: *ibid.*, at p. 132.

61. *Supra*, p. 7.

62. Y. CARON, « De l'action réciproque du droit civil et du *common law* dans le droit de compagnies de la Province de Québec » in *Studies in Canadian company law*, vol. 1, at p. 104.

63. See also: *Perrault v. Central Agency* (1924) 37 Que. K.B. 305 at p. 308. The older *Companies Acts* of the province often made this same distinction: e.g., *Companies Act* (1920) 10 Geo. V c. 72 articles 5962a, 5963 and 5968.

when one turns to the Commissioners' *Reports*, the reason for this becomes apparent. The Commissioners, in drafting article 1889 C.c., referred exclusively to English sources where the distinction is a valid one⁶⁴; however, they indicated in their commentaries under this article that they doubted whether in fact any such companies had ever existed in Quebec⁶⁵.

Most Quebec writers have accepted this proposition⁶⁶ and the consensus has been, for more than a century, that in fact unincorporated joint-stock companies were not to be found in the Province.

When one considers that such companies existed in Upper-Canada⁶⁷, this casts serious doubts on the generally accepted theory. Recent research in economic history and even a handful of cases from our provincial courts will give us clear examples of unincorporated joint-stock companies formed in Quebec that were ultimately regulated by adequate provincial legislation. Contrary to the traditional views, it will appear that the distinction set out in article 1889 C.c. is not purely academic but historically and factually correct.

a) Unincorporated joint-stock companies for the purposes of colonization: 1791-1809

As early as the late eighteenth century, unincorporated companies made their appearance in Quebec⁶⁸: mostly used for purposes of colonizing land, they had all the main characteristics of their English counterpart.

Thus, these companies had a capital that was divided into transferable shares⁶⁹. A trustee was owner of the property of the company for the same practical reasons as in English law⁷⁰. Also, the company was ad-

64. *Sixth Report*, vol. III: p. 31 of the Report and 130 of the Draft Code. The Commissioners referred to: Collyer, Gow and Story.

65. *Ibid.* Thus, they commented: « Il est douteux qu'il existe ici aucune société en opération sous la forme de sociétés par actions sans la sanction de l'autorité publique . . . » From the Report reproduced in C. de Lorimier, *Bibliothèque du Code Civil de la Province de Québec*, vol. 15, Cadieux & Derome, Montréal, 1886, at p. 156. *Vide* also: P.B. MIGNAULT, *Le Droit civil canadien*, vol. 8, Wilson & Lafleur, Montréal, 1909, at pp. 246-247.

66. SMITH et RENAUD, *op. cit.*, vol. I at pp. 27 and 36; J. SMITH, *Le statut juridique de l'administrateur et de l'officier au Québec* (1973) 75 R. du N. 530 at p. 535.

67. Risk, *supra* n. 54 at p. 300, n. 175. An illustration in the Ontario jurisprudence: *Comer v. Thompson* (1851) 4 U.C.Q.B. (o.s.) 256.

68. G. F. McGUIGAN, *supra* n. 26 at pp. 32 and 36.

69. *Ibid.*, at pp. 46-47, 50-51 and 55.

70. *Ibid.*, at pp. 51, 52-53 and 55. *Vide* also the following authorities: F. J. NUGAN.

ministered not by its members but by representatives chosen for this purpose⁷¹.

The existence of such companies can be traced to many sources. The first and most obvious one is the great influence of English commercial practices imported into Quebec by the new English settlers. Such companies were also known in New England⁷² and the arrival of the American Loyalists after the War of Independence must have increased their popularity⁷³. Finally, even the civil law tradition ultimately helped the introduction of such companies to Quebec: businessmen, under the French rule, had been accustomed to the simplicity of the *contrat de société* and probably were very critical of the formalism of royal charters. Unincorporated companies offered the same flexibility as civil law partnerships without the burdensome procedure attached to petitions of incorporation⁷⁴.

b) The unincorporated joint-stock company before the courts

Even in the jurisprudence of the Province one can find traces of the existence of unincorporated companies: cases on this type of association are rare⁷⁵ but they are of great importance. Illustrations taken from judgments reveal that the structure of the unincorporated company in Quebec was identical to its English model. Thus, in the case of *Loranger v. Dorion*⁷⁶, the notes preceding the judgment contain important references to the constitution and by-laws of an unincorporated company, the *Silver Plume Mining Company*: this case is the most typical one and warrants closer examination.

"Pre-Incorporation contracts", in *Studies in Canadian company law*, vol. 1, at pp. 204-205; C. FORTIN, *The pre-incorporation trust, a victim of misconstruction?* (1970) 30 R. du B. 78 at pp. 85 and 87.

71. McGUIGAN, *op. cit.*, at pp. 46-47, 47-49 and 55.

72. *Ibid.*, at pp. 39-41.

73. *Ibid.*, at p. 46.

74. *Ibid.*, at pp. 36-37; *vide also* COOKE, *op. cit.*, at p. 124.

75. The only cases that the reports seem to yield are the following: *Bruneau v. Fosbrooke* (1851) 2 R.J.R.Q. 414 (S.C.); *Regina v. St-Louis* (1860) 10 L.C.R. 34 (Q.B.); *Prévost v. Allaire* (1861) 11 L.C.R. 293 (Q.B.); *Loranger v. Dorion* (1881) 4 L.N. 108 (S.C.) confirmed by the Court of Appeal at (1881) 4 L.N. 373 (Q.B.). Note that although the cases are rare, they are of some importance, having been decided in major part in the Appeal Court of the Province. See also, Labrie and Palmer, *op. cit.*, at p. 51 for another example.

76. *Ibid.* The company was also involved in *Chrétien v. Crowley* (1882) 2 D.C.A. 385 (Q.B.).

The company was administered by a board of directors, among whom a president, vice-president and secretary were chosen: thus, the unincorporated company in Quebec had a traditional corporate administration⁷⁷. The board of directors also had the power to make by-laws⁷⁸. The company had a share capital that was freely transferable: this is one of the great differences between the unincorporated company and the partnership of civil law⁷⁹. Finally, the presence of the trustee as owner of the capital stock of the company⁸⁰ and the person responsible for all transfers of shares⁸¹ indicates that such companies were similar to the unincorporated bodies that appeared in England after the *Bubble Act*.

However, the English influence was to be checked by the Courts: common law institutions could not easily be integrated into the economy of civil law rules and for that reason the provincial courts constantly tried to force the unincorporated company into a civilian category. The few cases reported clearly show that every time the courts had to deal with the relationship of members of unincorporated companies *inter se* or with third parties, they considered them as members of ordinary civil law partnerships⁸² and refused to apply to them any special regimen. Thus, the civil law was to assimilate the unincorporated company and transform it into a creature of its own⁸³.

77. *Ibid.*, at p. 109. See also: *Prévost v. Allaire*, *supra* n. 75 at pp. 310 and 313; *Regina v. St-Louis*, *supra* n. 75 at p. 35, and *supra* n. 71.

78. *Ibid.*, at p. 109.

79. *Loranger v. Dorion*, *ibid.*, at p. 109; *Regina v. St-Louis*, *supra* n. 75 at p. 35.

80. In the *Loranger* case, all of the capital stock of the company was to be issued to a trustee who would be in charge of transfers: *supra* n. 75 at p. 109. This was clearly set out in article 22 of the constitution and by-laws of the company. See DU BOIS, *op. cit.*, at p. 222. Trustees are often used in early legislations, a fact that betrays the great influence of English law: Fortin, *supra* n. 70, at p. 91; Labrie and Palmer, *op. cit.*, at pp. 53-54. Unincorporated companies in Quebec made use of the trustee as early as the late eighteenth century: *vide* MCGUIGAN, *supra* n. 70. Note, however, a major difference between Quebec law and that of England: in most English joint-stock companies, the association is administered often by a group of trustees rather than by a single one (*supra* n. 30) whereas in Quebec, it is rare to find in such companies more than one trustee. This was probably due to the primitive nature of most unincorporated companies in the province.

81. *Ibid.*

82. *Bruneau v. Fosbrooke*, *supra* n. 75 at p. 414; *Regina v. St-Louis*, *ibid.*, at pp. 41-42; *Prévost v. Allaire*, *ibid.*, at p. 301. *Vide* also H. ROCH et R. PARÉ, *Traité de droit civil du Québec*, vol. 13, Wilson & Lafleur, Montréal, 1952, at p. 451.

83. The cases do not discuss the particular rules applicable to the trustee of unincorporated companies. Should he be governed by the rules of common law or should he be subjected to the principles of the Civil Code? Although there were no cases settling the question as far as the trustees of unincorporated companies were concerned, cases suggest constantly that the law of the Province does not know of rules of Equity or

This tendency in Quebec to relate particular rules of company law to the more general principles of civil law becomes more apparent when one examines the special legislation enacted to control this new form of commercial association.

c) The Legislator intervenes

i) Information concerning unincorporated bodies

In English law, the legality of unincorporated companies has always been open to some doubt⁸⁴. In Quebec law, however, such companies are perfectly legal. Thus, article 1889 C.c. implicitly admits that « rien n'empêche . . . que les associés divisent leur capital en actions et souscrivent chacun un certain nombre d'actions . . . »⁸⁵. However, when an unincorporated company is formed in Quebec, article 1889 C.c. declares that it is considered as a general partnership⁸⁶; consequently, the liability of the members of such bodies is unlimited, as set out in articles 1854 and 1865 C.c.⁸⁷. Unincorporated companies, in theory, could still be formed under Quebec law but they would simply be considered as a species of partnership.

Trust and that where one finds statutes that refer to such common law institutions all efforts must be made to try to understand such mechanisms according to civil law rules. Thus, the courts have refused to admit the principles of trust in the law of the Province: on this point, see the interesting discussion in *The Corporation of the County of Drummond v. The South Eastern Railway Co.* (1878) 22 L.C.J. 25 (S.C.) at p. 32; (1879) 24 L.C.J. 276 (Q.B.) at pp. 284-285. For a modern restatement of this rule see: *Laliberté v. Larue* [1931] S.C.R. 7, at pp. 17-18.

84. GOWER, *op. cit.*, at p. 37; Risk, *supra* n. 54 at p. 300 n. 175; COOKE, *op. cit.*, at pp. 106-109, 128. *Vide* also DU BOIS, *op. cit.*, at p. 236. Equity however did not hesitate to protect the members of such bodies: see DU BOIS, *op. cit.*, at pp. 227-228, where the author illustrates this proposition with an unreported case, *Hollis v. Childe*, that lasted 70 years. *Vide* also CARR, *op. cit.*, at p. 191.

85. MIGNAULT, *op. cit.*, vol. 8 at pp. 246-247; F. LANGELIER, *Cours de droit civil*, vol. 6, Wilson et Lafleur, Montréal, 1911, at p. 62. ROCH et PARÉ, *op. cit.*, at p. 451; V. E. MITCHELL, *A treatise on the law relating to Canadian commercial corporations*, Southam Press Ltd., Montréal, 1916, at pp. 23 and 83.

86. 1889 C.c. reads, *in fine*, as follows:

"Joint-stock companies . . . are formed without such authority, and in the latter case, are subject to the same general rules as partnerships under a collective name."

This refers to general partnerships, dealt with in articles 1865-1869 C.c. Note that in French they are described as "sociétés en nom collectif" which is the reason why article 1889 C.c. mentions collective as opposed to general partnerships: the latter is the correct appellation and the wording of article 1889 C.c. in the English version on this point is a mere variation.

87. *Vide*, generally, *supra* n. 85.

The legality of such companies was also recognized as early as 1849: thus, by the Union statute of 12 Vict. c. 45, entitled *An Act to facilitate actions against persons associated for commercial purposes and against unincorporated companies*, members of such companies had to declare the composition of their association in order to allow for personal actions against them if the company should default⁸⁸. This statute is the origin of the present *Companies and Partnerships Declaration Act*⁸⁹. The Act of 1849 also equated the unincorporated company with an ordinary civil law partnership and the individual liability of the members of such bodies declared by the statute was to be confirmed by subsequent jurisprudence⁹⁰.

Thus, the Act of 1849 reveals that unincorporated companies existed at that early period and that their legality was not doubted even then by the Legislator. It also illustrates the typical reaction of jurists in Quebec law when faced with common law institutions: by assimilating them to the rules of civil law, they have tried to preserve harmony in the legal system of the Province⁹¹.

88. Article 5 of the Act declares that the word "société" includes the unincorporated company, and article 6 limits the application of the Act to Lower-Canada (Quebec).

89. R.S.Q. 1964 c. 272, section II. The 1849 Act has had a long history. See: (1856) 19-20 Vict. c. 52; (1859) 22 Vict. c. 4; (1860) C.S.L.-C. c. 65 and after the Confederation: (1885) 48 Vict. c. 29; R.S.Q. 1888 art. 5635 and following; R.S.Q. 1909 art. 7437 and following; (1924) 14 Geo. V c. 62; R.S.Q. 1925 c. 224; R.S.Q. 1941 c. 277 until it finally became c. 272 of the R.S.Q. 1964. A similar obligation was imposed upon incorporated companies but they had to furnish information by virtue of a different statute: (1876) 40 Vict. c. 15 am. by (1882) 45 Vict. c. 47. Companies which failed to file the necessary declarations were not as a consequence prevented from contracting validly nor were their charter powers destroyed: *Lippes v. Tutt* (1926) Que. K.B. 566, at pp. 574-575 per Greenshields, J. Note that the consolidation of 1925 merged both statutes and the obligation was imposed on all bodies forming commercial associations: R.S.Q. 1925 c. 224. See also: (1924) 14 Geo. V c. 62. An interesting analysis of the statute can be found in SMITH et RENAUD, *op. cit.*, vol. 3, at pp. 1714-1718.

90. In *Prévost v. Allaire*, *supra* n. 75, Aylwin, J., reminds us that unincorporated companies cannot carry on business without declaring their membership: *ibid.*, at p. 319. The court also points out that in the case of such bodies, the liability of members is unlimited: *per Mondelet, J.*, at pp. 322-323 and *per curiam* at p. 324. The same rule prevailed in English law: COOKE, *op. cit.*, at pp. 176-177; Du Bois, *op. cit.*, at pp. 222-226.

91. *Vide supra* n. 83.

ii) *Quo warranto*

In 1849, the Legislator enacted the statute 12 Vict. c. 41⁹² which codified prerogative writs⁹³ and *inter alia*, at article 8 of that Act, the rules concerning *quo warranto*⁹⁴: from then on, any body assuming to act as a corporation was to be declared illegal⁹⁵. One wonders if that particular section was intended to apply to unincorporated companies at the time.

As established previously, unincorporated companies are perfectly legal in civil law⁹⁶. They become illegal only when they contravene the rules of *quo warranto*, now set out in article 828 C.c.p. and more particularly the first paragraph thereof:

"828. The Attorney General may take action, according to the ordinary rules, to ask that the sanctions provided by law be imposed:

1. when a person, association or group of persons are acting as a corporation without having been legally incorporated or recognized as such; . . ."

What is meant, in our law, by the expression "acting as a corporation"?

There is only one reported case from the Courts that has given any attention to this matter and that is *Loranger v. Dorion*⁹⁷. That was a case dealing with an unincorporated company⁹⁸ and the court decided that it

92. The title of this statute was: "An Act to define the mode of proceeding before the Courts of Justice in Lower-Canada, in matters relating to the protection and regulation of corporate rights and Writs of Prerogative . . .".

93. *Ibid*; F. W. WEGENAST, *The law of Canadian companies*, Burroughs & Co., Toronto, 1931, at p. 87.

94. The law was enacted to deal with cases where "any association shall act as a corporation without being legally incorporated . . ."; WEGENAST, *ibid*. In old English law, *quo warranto* was the appropriate remedy in cases where persons pretended to act as a corporation when in fact they had never been legally constituted as such: J. GRANT, *A practical treatise on the law of corporations*, Butterworths, London, 1850, at pp. 41 and 282. However, such remedy applied only to cases where public franchises were abused and the writ never issued in cases of private corporations: GRANT, *op. cit.*, at pp. 282-283. In Quebec law, *quo warranto* issued in both cases, i.e., where persons pretended to act as a private or a public corporation: *Loranger v. Dorion*, *supra*, n. 75. See also: SMITH et RENAUD, *op. cit.*, vol. 3, at pp. 1810-11, 1819-20.

95. 12 Vict. c. 41 art. 8. Note that in English law, for an unincorporated body falsely to represent that it had been duly incorporated was a criminal offence at common law: CARR, *op. cit.*, at p. 116 n. 2; also at p. 171. What exactly constituted acting as a corporation in English law was a doubtful question: *Loranger v. Dorion*, *supra* n. 75, at p. 109 *per* Torrance, J.; *supra* n. 84, and authorities cited.

96. *Supra*, pp. 350-351.

97. (1881) 4 L.N. 108, 373.

98. The Silver Plume Mining Company: see the discussion, *supra*, at pp. 348-349.

had in fact acted as a corporation, arguing that "...a society which arrogates to itself this character of independent personality does assume to act as a corporation . . ."99. However, the facts of the case indicate the true limits of this decision. The company possessed a seal¹⁰⁰ and was administered by a board of directors who had the power of making by-laws¹⁰¹. It also had a capital divided into transferable shares¹⁰² but, above all, in its documents it styled and represented itself as a duly incorporated company, which in fact it was not¹⁰³. Under the circumstances, the Court held that the company was acting illegally as a corporation¹⁰⁴.

One can question whether the same conclusion would have been arrived at if the company had not made the representation that it was incorporated. In Quebec law, the possession of a corporate seal is of little importance¹⁰⁵. Administration of a body by certain elected representatives is not the exclusive privilege of corporations¹⁰⁶ and nor is a freely transferable stock¹⁰⁷. Thus, the company's misrepresentation seems to have been the ultimate factor that rendered, in *Loranger v. Dorion*¹⁰⁸, the unincorporated company an illegal association¹⁰⁹. If such representation had not been made, it is submitted that the company would not have fallen within the application of the *quo warranto* rules.

Unincorporated companies in Quebec are perfectly legal associations, recognized by article 1889 C.c. It is only when they assume the character of independent personality, when they represent themselves as bodies corporate, that *quo warranto* proceedings may be initiated against them.

The presence of unincorporated companies in a civil law jurisdiction betrays the considerable influence that English law exercised on our

99. Torrance, J., at p. 109.

100. *Ibid.*

101. *Ibid.*

102. *Ibid.*

103. *Ibid.* Thus, article 1 of its constitution declared that the company in that case was a corporation.

104. *Ibid.*

105. Article 33 of the *Companies Act*; M. et P. MARTEL, *Aspects juridiques de la compagnie au Québec*, vol. 1, Publications Les Affaires Inc., Montréal, 1972, at p. 131; CARR, *op. cit.*, at p. 55: "A body which possesses and uses a common seal is not necessarily a corporation . . ." Cf. SMITH et RENAUD, *op. cit.*, vol. 3, at p. 1819.

106. E.g.: article 1871 and following of the Civil Code.

107. *Supra* n. 85.

108. *Supra* n. 75.

109. *Ibid.*, at p. 109; CARR, *op. cit.*, at pp. 6, 28-29.

commercial institutions even before the adoption of a *Companies Act*¹¹⁰. To this day, the Civil Code still refers at article 1889 C.c. to the possibility of creating such companies: although this would seem highly improbable if not impossible¹¹¹, it remains a clear indication of the impact of the English presence on our system of laws.

II. Enter the pre-incorporation trust

Article 29 of the *Companies Act* reads in part as follows:

"The company . . . shall forthwith become and be vested with all property and rights, moveable and immoveable, held for it up to the date of the letters-patent, under any trust created with a view to its incorporation . . ."

In recent years, considerable discussion has centered on the origin and meaning of what one commentator has described as "the most enigmatic piece of legislation . . ."¹¹² to be found in our *Companies Act*. The first part of this discussion will deal with the historical origin of the section before examining in the second part the application of the pre-incorporation trust to promoters in the civil law of the Province.

A. A "NEBULOUS" ORIGIN¹¹³

The unincorporated company, as established previously, centered on the trustee: even in Quebec, the unincorporated body made a timid appearance and its most striking feature there was the existence of a trustee in a civil law jurisdiction¹¹⁴. One theory put forward to explain the origin of article 29 was that this section was intended as a purely transitory measure: when the first general incorporation statutes were adopted for the whole of Canada, some mechanism was necessary to allow unincor-

110. SMITH et RENAUD, *op. cit.*, vol. I at p. 36; SMITH, *supra* n. 66 et p. 535.

111. The *Securities Act* prohibits trading in securities without being registered: articles 14 and 16 of the Act. The Securities Commission would probably refuse to register an unincorporated company that desired to issue shares on the market. It is interesting to note that in the *Loranger* case, *supra* n. 75, the company had even obtained a quotation on the Stock Exchange for its shares: it had not mentioned to the Board of the Stock Exchange that it was not incorporated. This does not appear in the report but details can be found in the Attorney-General's factum in the Court of Queen's Bench file n. 332 (18 June 1881) at pp. III and VIII. See also *Chrétien v. Crowley*, *supra*, n. 76 at p. 388.

112. J. Smith, *Duties and powers of promoters in the company law of the province of Quebec* (1973-74) 76 R. du N. 207 and 269 at p. 271.

113. C. FORTIN, *The pre-incorporation trust: a victim of misconstruction?* (1970) 30 R. du B. 78 at p. 83.

114. *Supra*, pp. 347, 348 et 349.

porated bodies desirous of acquiring the benefit of legal personality to transfer their property to the newly formed companies¹¹⁵. The owner of the unincorporated company's property was, at law, the trustee¹¹⁶, and it was from him that the property had to be transferred to the new company. This would explain the curious formulation of article 29 of the Act. This view has been accepted by the Ontario Legislature who subsequently repealed the section, treating it as a mere historical anomaly¹¹⁷.

Serious doubts have arisen concerning the validity of this interpretation: Professor Fortin has conclusively shown that although the approach is an ingenious one, it is completely wrong. The first general incorporation statutes in Canada did not even contain a similar section¹¹⁸: it is clear that the Legislator's intentions were not to facilitate a transition if in the first statutes no mention of a transition section is to be found¹¹⁹. Moreover, as Fortin argues, the trustee in an unincorporated company does not hold property "with a view to its incorporation"¹²⁰ but for merely practical reasons¹²¹. After an extensive review of the early incorporation Acts in England and Canada, Professor Fortin comes to the conclusion that legislation of the type of s. 29 was not intended as a transition mechanism but must have been enacted for other purposes¹²².

But then, for what other purposes? Professor Fortin suggests that article 29 of the *Companies Act* was set out in order to solve the difficult problem of pre-incorporation contracts in Quebec law¹²³. However, he offers no authority for this proposition and bases his whole argument on pure conjecture. Thus, the author laments:

115. F. J. NUGAN, "Pre-incorporation contracts" in *Studies in Canadian company law*, vol. 1, at pp. 204-205.

116. *Ibid.*

117. *Interim Report of the Select Committee on Company Law* (Lawrence Report), Ontario, 1967 at p. 11, par. 1.5.4; SMITH, *supra* n. 112 at pp. 271-272.

118. FORTIN, *supra* n. 113 at pp. 84-86, where the author shows that in England, for example, the first registration statute did in fact contain clear transitory sections: (1844) 7-8 Vict. c. 110 s. 25. However, in Canada the very first statutes of 1850 and 1864 contained no such sections: *ibid.*, at pp. 85-86, 88. The author refers to the following Acts of the United Parliament: (1850) 13-14 Vict. c. 28 and (1864) 27-28 Vict. c. 23.

119. FORTIN, *ibid.*, at p. 90.

120. *Ibid.*, at p. 89.

121. *Ibid.* It is indisputable that unincorporated companies were formed because it was so difficult to obtain charters generally: *supra*, pp. 7-9. Consequently, the trustee of such bodies did not hold the company's property in the hope that one day it might become a corporation at law. Trustees held the property to simplify rules of procedure and not for this more doubtful purpose. *Vide supra* n. 31.

122. FORTIN, *supra* n. 113 at p. 91.

123. *Ibid.*

"... we have to rest our opinion as to the *raison d'être* of this section on probabilities concerning immediate or circumstantial causes which promoted and surrounded its adoption, as well on previously expressed opinions on the matter . . ."¹²⁴.

The jurisprudence of our Province, as will be seen later on, has accepted the view that s. 29 deals with a matter of promotion but it is important to stress the fact that no authority can be found establishing historically that the section was intended as such¹²⁵. This problem will now be examined with more attention.

The first *Companies Act* applicable to the Province after Confederation was enacted in 1868¹²⁶. When one examines closely the various sections of the provincial Act, certain conclusions on the origin of s. 29 become inevitable. Thus, s. 4 sets out the various details that must be included in the petition for incorporation. *Inter alia*, ss. 4(2) declares that the petition must set out the amount of capital subscribed by the petitioners, the payment made thereupon and the mode of payment. Ss. 4 (3) requires that at least 50% of the nominal capital be subscribed for and ss. 4 (4) declares that 10% of the subscribed capital must have been already paid in¹²⁷.

This information is contained in the petition for incorporation—evidently, at that point, the company is not in existence. Consequently, one wonders who will hold, until incorporation, the monies required to be paid upon the capital before a charter can be granted. Article 4 (5) of the same Act gives a clear answer to the question:

"Such aggregate must have been paid in to the credit of the company, or of trustees therefor, and must be standing at such credit, in some chartered bank, or banks within the province, unless the object of the company is one requiring that it should own real estate, in which case not more than one half thereof may be taken as invested in real estate suitable to such object, duly held by trustees therefor . . ."

Thus, trustees will hold the monies and the property of the company until its incorporation, when, as article 8 declares, the company will be-

124. *Ibid.*, at p. 84. The only serious authority referred to by Fortin is Wegenast where the author agrees with Fortin's conclusions but does not discuss the question of the origin of the section at all: *vide* WEGENAST, *op. cit.*, at p. 262. For another interesting speculation on the origin of the article: MARTEL, *op. cit.*, vol. 1, at pp. 48-49.

125. SMITH, *supra* n.112 at pp. 271-273, agrees with Fortin's views but does not add anything new to the arguments put forward by the commentator.

126. (1868) 31 Vict. c. 25.

127. Or at least 5% of the total nominal capital: *ibid.*, ss. 4 (4).

come vested with such rights from the moment it receives its letters-patent¹²⁸.

As a consequence, the origin of article 29 can be explained as follows: in the first general incorporation laws of our Province, before the letters-patent were granted to petitioners, certain requirements as to capital had to be met. One such requirement was that there had to be a *minimal paid-up capital for the protection of investors generally*¹²⁹. The company not being in existence, such monies had to be held in trust until its incorporation, when it would automatically become vested with the property held for it by the trustees.

The minimal capital requirement had a curious history: it was repeated in the consolidation of 1888¹³⁰ but disappeared in 1907¹³¹ as a condition precedent to incorporation. However, although the requirement disappeared, the reference to the pre-incorporation trust remains to this day on the statute books, causing considerable perplexity¹³².

There is very little jurisprudence on the statutory trustee charged with holding the minimal capital before the company's incorporation. There is however one interesting case dealing with the nature of his relationship to the promoters of a company. In *Bonhomme v. Bickerdike*

128. Note that Professor FORTIN, *supra* n. 113 mentions at pp. 86-87 that the Union statute of 1864 contained a similar section and wonders, at p. 89, if this could be an explanation as to the origin of the section. However, he does not discuss the possibility any further nor does he examine the provincial Act in this respect.

129. As to the intention of the Legislature in enacting such requirements, *vide infra* n. 145.

130. R.S.Q. 1888 s. 4698 (5) and 4705.

131. S.Q. (1907) 7 Ed. VII c. 48. At that point, the requirement that a minimal paid-up capital be in existence before the issuance of the letters-patent disappeared, but somehow the vesting provision remained on the statute books (S.Q. 1907 c. 48 s. 21). This was not such an absurdity as it may seem: in fact, article 6g of the 1907 statute declares that the petition for incorporation must set out "... the amount of stock ... the manner in which the same has been paid, and is held for the company ...". If this means, *in fine*, that the money of the pre-incorporation subscriptions might be held for the company by trustees thereof, then this justifies the mention at article 21 of the Act that on incorporation the company becomes vested with such property. Article 6g became article 6007 of R.S.Q. 1909, but the reference to "the manner in which ... [the money] ... is held for the company" disappeared finally in (1920) 10 Geo. V c. 72, art. 5962g. Thus, the existence of the pre-incorporation trustee from 1868 to 1920 justified the vesting provision that is now reproduced in s. 29 of the Act. However, after 1920, s. 29 became a mere historical anomaly that should have been removed from the Act.

132. The jurisprudence of the Province, not taking into account the historical origin of this type of legislation, simply applied it, as we shall see, to a pre-incorporation contract situation: *vide* SMITH et RENAUD, *op. cit.*, vol. I at p. 87.

¹³³, the defendant was one of the trustees who held the minimal capital pending the future company's incorporation¹³⁴. In the Court of Review, Cimon, J., held that trustees under the statute were not promoters of the company as such: on the contrary, they were merely mandataries of the promoters and it is on the latter that liability should be imposed when any damage is caused by the promotion of a company¹³⁵. However, in that case, the Court held that defendant was actually a promoter: this was not due to the simple assumption of the quality of trustee, but because he had participated actively in the promotion of the company¹³⁶. The defendant had controlled credit sales to the future company¹³⁷, had allowed his name to be used in the prospectus, which he also corrected and read¹³⁸, was a trustee of the company¹³⁹ and generally acted as a promoter. The Court, stressing the point that the determination of the question whether any person is or is not a promoter is always a question of fact, held the defendant liable for a variety of damages¹⁴⁰.

The principle that can be derived from the case is an important one: a pre-incorporation trustee under the old statutes was not a promoter of the company but at best an agent of the promoters. He could become a promoter if he participated in the general administration of the promotion but this was not a necessary incident of his original quality. Thus, the pre-incorporation trustee, at the outset, was not considered as a promoter when the courts were called upon to decide this question. It was only later cases that viewed him as such, without taking into consideration the historical explanation of his mention in the statute books.

133. (1900) 17 Que. S.C. 28 (C.R.). This case, in review, was confirmed by the Court of Appeal on the 24 April 1900 (unreported).

134. *Ibid.*, at pp. 32, 38, 49-50 and note at p. 51: « Le défendeur avait donc assumé ce mandat, au nom de la compagnie, de déposer et détenir ces argents, comme un des trustees de celle-ci . . . » (*per* Cimon, J., in the C.R.).

135. *Ibid.*, at pp. 43-44.

136. *Ibid.*, at pp. 51, 52 and 54.

137. *Ibid.*, at p. 54.

138. *Ibid.*, at p. 46.

139. *Ibid.*, at pp. 49-50.

140. *Ibid.*, at pp. 57-58; J. H. GROSS, *Company promoters*, Tel Aviv University, Tel Aviv, 1972, at p. 25. Thus a promoter, in Quebec law, can only be described as such if he carries on certain activities: an exhaustive definition is difficult to arrive at in such a case and a more general test, as suggested by this case, seems appropriate. On the definition of promoters generally in our Province *vide* SMITH, *supra* n. 112 at p. 210, referring to *Federated Press Ltd. v. L. H. Archambault* (1924) 30 R.L.n.s. 220 (S.C.). Note that in Quebec, one can still be a promoter of a company after its incorporation: *Pépin v. Dufour* (1925) 31 R.L.n.s. 446 (S.C.) at p. 449; GROSS, *op. cit.*, at p. 68; also at pp. 30, 32, 56-59 on the question of establishing when a promotion actually stops.

Minimal capital requirements were not to disappear completely but their importance was to become secondary. Whereas, until 1907, such a requirement was a condition precedent to incorporation, after that period it became a mere condition to be fulfilled before the company could start its operations¹⁴¹ but was no impediment to the granting of a charter. Requirements of minimal capital disappeared completely from the *Companies Act* in 1964¹⁴²; statutory protection of creditors and shareholders in general then became unnecessary in view of the active protection afforded by the *Securities Act* and the Commission established thereunder¹⁴³. Before that period, however, minimal capital requirements were

141. After 1907, a minimal paid-up capital was necessary before the company could start operating but it nevertheless obtained its charter before that moment: S.Q. 1907 c. 48 s. 18; R.S.Q. 1909 s. 6019; R.S.Q. 1925 c. 223 s. 23; R.S.Q. 1941 c. 276 s. 24.

142. Ab. by S.Q. 1964 c. 59 s. 4. The minimal capital requirement gave rise to some interesting jurisprudence in our Courts. Third parties were held to have constructive notice of this requirement: *Bergeron v. La Cie. de meubles de Jonquière* (1913) 22 Que. K.B. 341, at p. 346. The statute imposed liability on the directors who allowed a company to carry on business before the requirement was met. This liability resulted from statute: *Lefebvre v. Prouty* (1918) 54 Que. S.C. 490 at p. 495-496; *Pérusse v. Fuller* (1919) 55 Que. S.C. 254 (C.R.) at pp. 257-258; *Phoenix Assurance Co. Ltd. of London v. Lagueux* (1932) 38 R.L.n.s. 474 (S.C.) at p. 495; on appeal at (1932) 53 Que. K.B. 398 at pp. 403 and 405; *Latreille Gaz Naturel Equipement Co. Ltd. v. B.C.N.* [1967] Que. Q.B. 259 at p. 261; *Caplan v. Alexis Nihon Co. Ltd.* [1966] Que. Q.B. 377 generally and more recently, *Schlesinger v. Employers' Liability Ass. Co.* [1972] Que. C.A. 65, at p. 66. The liability might also result from the general principle of delict set out in article 1053 of the Civil Code: where a statute directs that a certain thing shall not be done, a delict is committed by him who acts in contravention thereof: *Lagueux* case, *supra* in (1932) 53 Que. K.B. 398 at p. 407.

If the company commenced business before the requirement of the Act was met, it could have its charter forfeited: *Grandbois v. Business Directory Services Ltd.* (1924) 62 Que. S.C. 213 at p. 214, 215-216; *The Queen v. The Eastern Archipelago Co.* (1853) 118 E.R. 988, 994. Note, however, that the requirements were not so drastic as to include preliminary contracts indispensable to the formation of the company: *Bégin v. William Copping Lumber Co.* (1923) 28 R.L.n.s. 399 (C.R.) at pp. 400-401.

143. The *Companies Act*, in the earlier years of this century, contained a myriad of sections dealing with the protection of the capital of the company: with the advent of modern securities legislation in the province, these sections proved of little importance in contrast to the more active role played by the Securities Commission as protector of investors. On this point, see the penetrating discussion in *In re Richelieu Oil Ltd.* [1950] Que. K.B. 714 at pp. 719-722. In England, surprisingly enough, minimal capital requirements have reappeared in the statute: GOWER, *op. cit.*, at pp. 300-301. They were introduced by the *Companies Act*, 1900: Pennington, *op. cit.*, at p. 255, and also at pp. 256-257. C.M. SCHMITTHOFF and J.H. THOMPSON, *Palmer's Company Law*, 21st ed., Stevens & Sons, London, 1968, at p. 184 n. 4 where the authors give a good *résumé* of the legislation and the evils it sought to cure. *Vide also Companies Act* (1900) 63-64 Vict. c. 48 (U.K.) s. 4 which became s. 47 of the *Companies Act*, 1948. In England, such provisions can be justified: the fact that investors cannot look to a Securities Commis-

set out in the statute for the protection of the public: as pointed out by Archer, J., in the Superior Court decision of *French Gas Saving Co. v. Desbarats*¹⁴⁴, the requirements of a minimal capital were instituted in order to protect the investing public against fraudulent promoters¹⁴⁵. Thus, if trustees held monies and property for that purpose, can one argue that the pre-incorporation trust was intended as a promotion mechanism when jurisprudence tells us that its main purpose was to protect investors against scheming promoters?

In final analysis, the origin of s. 29 can simply be explained by the fact that until 1907, the provincial *Companies Act* required that minimal capital be paid up and held by trustees as a condition precedent to incorporation¹⁴⁶. When that condition was abolished in 1907, article 29 of the Act should have been amended in consequence: the failure to do so was to cause a great deal of confusion and disputation among the legal commentators of the Province.

B. THE PRE-INCORPORATION TRUST IN CIVIL LAW

The courts of the Province, more than eager to find some adequate solution to the problems of pre-incorporation contracts, gladly seized upon s. 29 of the Act and turned it into a promotional device¹⁴⁷. A great

sion for adequate surveillance of company promoters generally explains the necessity of such statutory safeguards.

144. [1912] 1 D.L.R. 136 (K.B.).

145. *Ibid.*, at p. 146. Such legislation was enacted for the protection of the public against the fraud of promoters: MITCHELL, *op. cit.*, at pp. 268 and 319; TASCHEREAU, J., in *Dominion Salvage & Wrecking Co. Ltd. v. The Attorney-General of Canada* (1892-93) 21 S.C.R. 72 at pp. 89-90 referring to *The Eastern Archipelago case*, *supra* n. 142; G. H. EVANS Jr., *British Corporation Finance 1775-1850*, The John Hopkins Press, Baltimore, 1936, at p. 100.

146. The use of a trustee to hold monies for the company to be incorporated somehow subsisted in commercial practices in the Province. Thus, in the recent case of *Latreille Gaz Naturel Equipement Cie Ltée v. B.C.N. & Lalonde* [1967] Que. Q.B. 259, L. held money for the plaintiff company in an account with the defendant bank: this account was "in trust" for the future company. However, in this instance, such trust did not refer to that mentioned in s. 29 of the *Companies Act*. "In trust" bank accounts are now quite familiar in Quebec law, where they have generated endless controversies in the courts and the textbooks as to their meaning in a civil law context. For an illuminating exposition of this complicated problem, *vide*: RENAUD et SMITH, *op. cit.*, vol. 2, at pp. 799-814. Note that in the aforementioned case, at p. 261, the Court held that such a trust—if it existed—would, under the circumstances of the case, justify an accounting on the defendant's part. This squares with the rule of 981 / C.c., imposing upon the trustees of civil law a duty to account to the beneficiaries.

147. Smith, *supra* n. 112 at p. 273.

number of cases have appeared of late¹⁴⁸ dealing with that particular piece of legislation in the context of pre-incorporation contracts without inquiring as to the historical validity of this process. In a sense, this approach has been beneficial and it can be argued that the error of historical interpretation was ultimately useful in this field.

As a promotional technique, the pre-incorporation trust has proven to be of some value: from the taxation point of view, it presents undoubted advantages¹⁴⁹ while offering at the same time a comprehensive solution to the problems of pre-incorporation contracts and the duties of promoters in the province of Quebec. Before examining these various points, some considerations on the nature of such trusts in civil law have to be set out.

1. *The pre-incorporation trust: a question of interpretation*

The statutory trust enacted by s. 29 of the Act presents a major problem of interpretation: should it be governed by the principles of civil law trusts¹⁵⁰ or should English law apply?

One school of thought argues for English law¹⁵¹. The main basis for this position is an historical one: the pre-incorporation trust appeared as early as 1868 in our provincial laws¹⁵² whereas the civil law trust appeared only in 1879¹⁵³. Consequently, English law must have applied at the time and should still be referred to in cases falling under s. 29¹⁵⁴.

This view has been severely criticized. Professor Smith has conclusively shown that even prior to 1879, trusts in Quebec law were interpreted according to civil law principles¹⁵⁵ and that even after that period,

148. *Ibid.*, at p. 273 n. 93.

149. W. M. FRIEDMAN, *The New Tax Act and the transfer to a corporation of assets acquired pending incorporation* (1973) 33 R. du B. 17 at pp. 25-26; FORTIN, *supra* n. 113 at pp. 100-101 and D. SOHMER, *The closely held corporation in 1972 jurisprudence* (1973) 33 R. du B. 122 at p. 132 n. 25 for other aspects of tax rebates possible with the use of pre-incorporation trusts.

150. 981a C.c. and following. Generally, on this very controversial subject, *vide* P. E. GRAHAM, *Some peculiarities of trusts in Quebec* (1962) 22 R. du B. 137; A. J. McCLEAN, *The common law and the Quebec trusts — some comparisons* (1967) U.B.C.L. Rev.-C. de D. 333.

151. MARTEL, *op. cit.*, vol. I at p. 47-48; SOHMER, *supra* n. 149 at p. 131 n. 32 where the author refers to G. W. KEETON, *Law of trusts*, 9th ed., Pitman, London, 1968, at p. 17.

152. *Supra*, pp. 356-357.

153. (1879) 42-43 Vict. c. 29.

154. *Supra* n. 151.

155. Smith, *supra* n. 112 at pp. 273-274.

the Courts have always refused to import English law on this subject¹⁵⁶. Recent research confirms and strengthens Smith's views¹⁵⁷.

After settling this issue, the learned author then concludes:

"The meaning of the word "trust" used in section 29 of the *Companies Act*, therefore, relates to a civil law concept. It is merely a label given to a legal relationship recognized by the law of Quebec . . ."¹⁵⁸.

This is where Professor Smith's reasoning becomes more difficult to follow. Smith argues that although the trust should be understood according to civil law, he does not establish what category of that law should apply. This question is an essential one: the nature of the trust created under s. 29 of the Act must be ascertained in order to allow for the imposition of rights and duties on the trustee and to establish the general rights of the company towards the latter¹⁵⁹.

There is no jurisprudence on this exact point but the following case is of great help in dealing with this problem. In *Laliberté v. Larue*¹⁶⁰, Rinfret, J., was discussing the nature of statutory trusts in the law of Quebec¹⁶¹: the learned judge was of the opinion that such trusts must be understood according to the rules of civil law¹⁶² and more particularly the rules of *Trusts* as set out in the Civil Code of the Province:

« . . . Il est impossible de ne pas voir l'analogie entre ces articles du code et le statut que nous étudions. Il est naturel et logique que nous en tenions compte . . ."¹⁶³.

The *Laliberté* case yields a precious tool of legislative interpretation in that the Supreme Court suggests that whenever the statute books of the Province refer to the concept of trust, such concept must be understood according to the private law of the Province as codified in the Civil Code. Thus, it is submitted, the rules of civil law must be resorted to in the case of the statutory trust under s. 29 of the Act: on the basis of the analogy

156. *Ibid.*, referring to *Laliberté v. Larue* [1931] S.C.R. 7 at p. 18.

157. D. N. METTARLIN, *The Quebec trust and the civil law* (1975) 21 McGill L.J. 175 at pp. 203-206.

158. Smith, *supra* n. 112 at p. 275.

159. *Komery v. Restaurant Komery Inc.* [1965] Que. Q.B. 853, at p. 856.

160. *Supra* n. 156.

161. The case dealt with the meaning of the trust created under the *Special Corporate Powers Act* R.S.Q. 1964 c. 275 s. 22 and following.

162. *Supra* n. 156 at p. 18.

163. *Supra* n. 156 at pp. 20-21. Rinfret, J., refers to *O'Meara v. Bennett* reported at [1922] A.C. 80 (P.C.) at p. 85. The trust analogy has also been suggested by the provincial Court of Appeal in *Yuksel Atillasoy v. Crown Trust Co.* [1974] Que. C.A. 442 at pp. 449, 451 but note that this was not a case of a statutory trust but a contractual one. See also, *infra* n. 258.

suggested by Rinfret, J., in the *Laliberté* case, the trust of s. 29 should be analysed according to the rules set out in the chapter *Of Trusts* in the Civil Code, whenever applicable. This should solve theoretically the problem of imposing duties on promoters in Quebec who organize corporate promotion by way of trust deeds under s. 29 of the Act¹⁶⁴.

2. The pre-incorporation trust: creation

Before the chapter on Trusts was inserted in the Civil Code in 1879¹⁶⁵, it was possible to create a trust for a company not yet in existence if there were trustees to hold the rights established under such a trust for the future company. In *Desrivières v. Richardson*¹⁶⁶, a legacy to trustees of a future corporation was being questioned as to its validity and Kerr, J., in the provincial Court of Appeal, confirmed the legality of such a trust:

"... for though it is admitted that a legacy is lapsed . . . when left to an individual, or to a body politic or corporate, not *in esse*, yet the principle does not apply to this case, inasmuch as the trustees were all alive when the testator made his will, and they received the bequest for the benefit of the Royal Institution so soon as it should please the Provincial government to give to 'airy nothing a local habitation and a name . . .'"¹⁶⁷.

This practice was taken from old English law¹⁶⁸ and its validity was to be once again confirmed by the courts half a century later¹⁶⁹. It would seem, however, that since 1879 this method is no longer possible: if a bequest is to be made to a corporation not *in esse*, the only way this can be done is under article 981a C.c., which sets out the conditions for creating a trust in civil law¹⁷⁰. Alternatively, a trust could be set up under s. 29 of the *Companies Act* and it is the requirements of form necessary under that statute that will now be examined.

164. The problem of promoters' duties in Quebec law remains unresolved to this day: SMITH, *supra* n. 112 at pp. 212 and 288. But see *infra*, pp. 372-373-381.

165. *Supra* n. 153.

166. [1826] Stu. K.B. 218 (Prov. C.A.), 224 (K.B.).

167. *Ibid.*, at p. 241.

168. *Ibid.* Note, however, that English law now refuses to admit the validity of a pre-incorporation trust: MARTEL, *op. cit.*, vol. I at p. 48; GROSS, *op. cit.*, at pp. 72-75 and pp. 77-78, 79 and more precisely at p. 86, where the author points to the "reasonable parallel" between the unborn child and the company prior to its incorporation; P. D. MCKENZIE, *The legal status of the unborn company* (1972-73) 5 N.Z.U.L.R. 211. American law recognizes the validity of such trusts: GROSS, *op. cit.*, at pp. 78-79. See also: FORTIN, *supra* n. 113 at p. 82.

169. *Abbott v. Fraser* (1874) 20 L.C.J. 197 (P.C.) at p. 216 *per* Sir Montague Smith, quoting with approval the *Desrivières* case, *supra* n. 166.

170. The trust of article 981a C.c. is subjected to various conditions of form: if it is a donation, it must be in notarial form (776 C.c.). As for trusts established by will, see art. 840 C.c. and following.

Section 29 does not give any indication as to the particular procedure that is necessary to create a trust thereunder: as a consequence, it is necessary to examine the requirements set out in the provincial jurisprudence and the commentators on this point.

The existence of a trust under s. 29 is a question of fact: the Courts have refused to infer from the conduct of the parties a trust in the name of a future company unless clear evidence that a trust had in fact been created is adduced¹⁷¹. Thus, in *St. Lawrence Clothing Manufacturing Co. of Quebec Ltd. v. Sun Insurance Office Ltd. of London*¹⁷², the declaration by a promoter that "... he was making the purchase for the account of a company about to be incorporated . . ."¹⁷³ was insufficient in the Court's opinion to bind the company¹⁷⁴. It was the Supreme Court of Canada's decision in *Provincial Hardwoods Inc. v. Morin & Al.*¹⁷⁵ that shed some light on this question. Fauteux, J., held that in order to prove the creation of a trust under s. 29 one had to establish the existence of a trustee who was acting for the benefit of a future company:

« Il est de l'essence d'un fidéicomis qu'un titre légal à des biens passe d'une personne à un fiduciaire qui le détient pour l'avantage du bénéficiaire du fidéicomis »¹⁷⁶.

Subsequent provincial cases on this issue followed the *Morin* principle and required that a very clear intention of acting as a trustee for the future company be proven before a trust under s. 29 was established: in *Hewlings v. Mirotchick*¹⁷⁷ a simple written declaration that one intended to act as a trustee was deemed insufficient by the Court¹⁷⁸.

171. *Komery v. Restaurant Komery Inc.* [1965] Que. Q.B. 853, *per* Brossard, J., at p. 857. Also *per curiam*, at p. 854.

172. [1943] Que. S.C. 144.

173. *Ibid.*, at p. 146, *per* Gibsone, J. In that case, it was established that such a declaration was made only once, although it was "said" that it was made in other cases: *ibid.*

174. *Ibid.*, at p. 148. Thus, the case is authority for the proposition that a simple passing reference will not constitute a trust under s. 29. However, other views on this case have been put forward and will be discussed later on: *infra*, pp. 368 and following.

175. [1966] S.C.R. 58.

176. *Ibid.*, at p. 67. Also at p. 66. SMITH, *supra* n. 112 gives an interesting analysis of the case at pp. 275-277, and more particularly at p. 276 n. 104 for a minor criticism of Fauteux, J.'s use of the expression « titre légal ». See also: GRAHAM, *supra* n. 150 at p. 142.

177. [1972] R.P. 22 (P.C.).

178. *Per* Gold, J., at p. 25, referring to the *Morin* case, *supra* n. 175. In the *Hewlings* case, perhaps if the promoter had declared expressly that he was acting as a trustee under article 29 of the *Companies Act*, the judgment could have been different. See also the recent decision of the Superior Court: *Guillemet v. Brazeau* [1973] Que. S.C. 953 at pp. 957-958, also referring to the *Morin* case.

There are several ways whereby one might be capable of establishing such an intention. In the decision of the Quebec Court of Appeal in *Giguère v. Bourque*¹⁷⁹, two promoters G. and V. prepared a written contract setting out that they intended to act as trustees for the future corporation¹⁸⁰; this agreement was sufficient according to the Court to create a trust under s. 29 and the company was held bound by the contracts subsequently entered into by its representatives¹⁸¹. The Court of Appeal, in another case¹⁸², suggested that the memorandum of association¹⁸³ might also be used to create a pre-incorporation trust indicating that if the intention of acting as trustee can be readily ascertained from a document then a valid trust under s. 29 will be created.

Another interesting approach is that proposed by Friedman¹⁸⁴. The author suggests that the trustee should register under the *Companies and Partnerships Declaration Act*¹⁸⁵; such registration is useful because of the publicity it gives to the creation of the trust¹⁸⁶.

S. 29 of the *Companies Act*, as interpreted by our Courts, creates a law of exception. Trusts, as we know them, are to be found only in the Civil Code¹⁸⁷ and declarations of trust in civil law are simply unknown¹⁸⁸; because s. 29 creates an exception to these two rules, courts have refused to interpret it liberally and will recognize a trust under s. 29 only when a clear intention of acting as a trustee for the future company has been established¹⁸⁹. This restrictive view is ultimately for the protection of the company: if the company is to be bound *in futurum* by mere declarations of intention, this could prove of serious consequence for the future shareholders and creditors of the company¹⁹⁰.

179. [1973] Que. C.A. 663.

180. *Ibid.*, at p. 664: « . . . en vertu d'un contrat de fidéicommiss . . . ».

181. *Ibid.*, at p. 667, *per curiam*.

182. *Komery v. Restaurant Komery Inc.*, *supra* n. 171.

183. *Ibid.*, at p. 857 *per* Brossard, J. The procedure of a memorandum of association was of course taken from English law: *Bergeron v. La Compagnie de meubles de Jonquière* (1913) 22 Que. K.B. 341 at p. 345.

184. *Supra* n. 149.

185. *Companies and Partnerships Declaration Act* R.S.Q. 1964 c. 272. Friedman, *ibid.*, at p. 24; the author suggests registration under s. 10 of the Act as "Sole Proprietor In Trust for a Corporation to be formed".

186. *Ibid.*, at p. 25.

187. 981a C.c. and following.

188. FORTIN, *supra* n. 113 at p. 91 n. 56 and p. 92. *O'Meara v. Bennett* [1922] A.C. 80 (P.C.); RENAUD et SMITH, *op. cit.*, vol. 2 at p. 807.

189. *Vide supra* n. 171.

190. The Court of Appeal has indicated in the *Komery* case, *supra* n. 171 that one of the main interests in establishing the nature of the relationship between a company and its

The majority of cases have thus taken a cautious approach to the pre-incorporation trust: there are, however, a few discordant views on this subject.

There is a curious body of jurisprudence that has taken the view that s. 29 applies to every case where the company purported to act before its incorporation¹⁹¹. The fact that the company is not in existence is described in one case as a purely "grammatical" nuance that should not prevent the imposition of obligations on the company¹⁹². Such views are open to serious criticism: surely if the Act mentions expressly a trust created with a view to incorporation, that must mean that some form of trust must at least exist before s. 29 comes into application. The reasoning of such cases is perhaps convincing from the point of view of equitable considerations, but it fails to take into account the nature of the corporate personality, the formulation of the *Companies Act* and the principles of law governing the relationship of promoters to the company in our Province¹⁹³. For these reasons, this minority view should be definitely set aside. The pre-incorporation trust, as a creature of jurisprudence, must meet with certain strict requirements and the most common *leitmotif* to be found in this context is clear proof of the intention of creating such a trust. This is best provided for in writing, although oral evidence would in principle suffice if admissible¹⁹⁴.

3. *The pre-incorporation trust: an exception to the rule in Kelner v. Baxter*¹⁹⁵

In Quebec, a company that is not in existence cannot as a consequence have any representatives: a civil law mandate cannot be created

promoters is the protection of third parties and creditors: *ibid.*, per Brossard, J., at p. 856. *Vide* also GROSS, *op. cit.*, pp. 172-173.

191. *St. Jovite Wood Products Inc. v. P. et L. Potvin & Cie.* [1962] Que. Q.B. 856 at p. 856 per Rinfret, J., diss. Note that the majority of the Court dealt with another question and Rinfret, J.'s view is merely *obiter*. *Komery v. Restaurant Komery Inc.*, *supra* n. 171 at p. 861 per Rinfret, J., dissenting again; *Gauvin v. Langelier* [1963] Que. Q.B. 206 at p. 207 per Choquette, J., where the judge based his decision on a partnership contract that he understood to be a trust under s. 29 although no mention of such trust was made in the contract.

192. *Per* Rinfret, J., in the *Komery* case, *ibid.* at p. 861.

193. SMITH, *supra* n. 112, has clearly shown that pre-incorporation activities will not bind the company unless some legal mechanism is invoked to justify this: see, generally, p. 217 and following.

194. The problem with oral statements is that they cannot vary the terms of a written contract: 1234 C.c.

195. (1866) L.R. 2 C.P. 174.

where there is no principal¹⁹⁶, and therefore, promoters cannot as agents bind the company before incorporation. Courts have applied this rule by invoking principles of civil law¹⁹⁷ but the majority of cases suggests that this is a mere duplication of the *Kelner v. Baxter* principle¹⁹⁸ and the latest authorities agree on this proposition¹⁹⁹.

Professor Smith's research has established, however, that the civil law offers in this context more protection to third parties than the common law²⁰⁰. The author has shown that a variety of mechanisms are available in civil law that allow for the imposition of liability on the company for pre-incorporation agreements. The rules of delegation²⁰¹, stipulation for the benefit of a third person²⁰², the conditional contract²⁰³, the theory of adoption of contractual liability²⁰⁴ and finally the rules of quasi-contract²⁰⁵, all serve the purpose of creating legal relationships with the company and a third party, once the company comes into existence.

The pre-incorporation trust is also considered as an available mechanism to that end by the learned author²⁰⁶; however, the considerable restriction imposed on the effect of the pre-incorporation trust by Smith's interpretation of s. 29 is so drastic that it warrants closer examination. The author argues that the company, on being incorporated, is not automatically bound by a contract made in its name by a trustee under s. 29: it must indicate its willingness to accept such contract and, as a

196. SMITH, *supra* n. 112 at p. 219. Anyone assuming the quality of mandatary in civil law where no mandator exists becomes personally liable on the contract: SMITH, *ibid.*, at pp. 214-216 discusses this point. See also: *Pearson v. Lighthall* (1895) 7 Que. S.C. 201 at p. 202; articles 1715-16 C.c.

197. SMITH, *ibid.*, at p. 219.

198. SOHMER, *supra* n. 149 at p. 130 n. 32. See also: *Chinic v. The Canada Steel Co.* (1876) 3 Q.L.R. 1 (C.R.) at p. 3; *Gadbois v. Montreal Exhibition Co. Ltd.* (1930) 36 R. de J. 478 (S.C.) at pp. 483-484.

199. *Guillemet v. Brazeau* [1973] Que. S.C. 953 at pp. 956-957, 958, and authorities therein referred to; *Dame Maria Klein-Schwartz v. Paul Powell et Empire Ethnic Pageantry* [1976] C. P. 24.

200. SMITH, *supra* n. 112 at p. 219.

201. *Ibid.*, at pp. 219-221. For a recent case where perfect delegation was invoked with success, see *Chapuis v. Banque canadienne impériale de commerce* [1975] C.A. 691.

202. *Ibid.*, at pp. 221-222. Note that in English law, such stipulations do not exist. Thus, Gross points out that the *jus quaesitum tertio* is unknown to common law: GROSS, *op. cit.*, at p. 184.

203. *Ibid.*, at pp. 222-224.

204. *Ibid.*, at pp. 224-226. See also: *De Bellefeuille v. La Municipalité du Village de St-Louis du Mile End* (1880) 4 L.N. 42 (S.C.) at p. 44.

205. *Ibid.*, at pp. 226-235 for a brilliant analysis of the application of the doctrines of unjust enrichment and *negotiorum gestio* in the field of pre-incorporation contracts.

206. *Ibid.*, at pp. 270-280.

consequence, can also repudiate it²⁰⁷. This extraordinary view of s. 29 is based on a reading of *St. Lawrence Clothing Manufacturing Co. of Quebec Ltd. v. Sun Insurance Office Ltd. of London*²⁰⁸ and Perrault's opinion of the case²⁰⁹. In view of the fact that it contradicts the express terms of s. 29 and that it renders the statutory trust completely useless in a pre-incorporation context²¹⁰, such an interpretation must be approached with some degree of scepticism. The case referred to by both authors is an old one and never actually refers to s. 29²¹¹. Moreover, the facts of the case do not justify the traditional views expressed on it. D. and L. wished to form a company and for that purpose approached legal advisers who commenced the necessary procedures. Meanwhile, D. was carrying on business in his own name: in January 1939, he purchased certain goods that were used exclusively for the purposes of his own business. In one case only, D. declared that he was making purchases for the account of a company to be incorporated²¹². At the same time, an insurance was taken on the goods bought by D. in January in the name of the future company²¹³. Letters-patent were issued on the 17 February and the next day fire destroyed D.'s premises with all the goods therein purchased during January. The insurance company refused the company's claim that it had an insurable interest and this was upheld by Gibsone, J., in the Superior Court:

"... in the opinion of this Court the purchase by Dorfman of the said merchandise as above related in January 1939, namely the purchase being made in his own name, and the merchandise shipped and delivered to him at his address, constitutes the said Dorfman the owner of such merchandise, and the fact that he may have mentioned to the sellers that his intention was that this merchandise should go to a company which was to be formed *did not affect the acquisition of ownership by D. personally* . . ."²¹⁴.

D. acquired the property in his own name and he alone had an insurable interest therein: the company that came in existence in February could not claim any rights. This essentially is what the Court decided.

The contention that it also decided that under a pre-incorporation trust the company must manifest its intention of accepting goods bought for it before its existence is not justified by the facts of this case nor by

207. *Ibid.*, at pp. 277-280.

208. [1943] Que. S.C. 144.

209. A. PERRAULT, *La Critique des Arrêts* (1943) 3 R. du B. 345.

210. SMITH, *supra* n. 112 at p. 280, where the author comments that "... the far-reaching implications of the wording used in this statute have been reduced to nothing . . ."

211. SMITH, *ibid.*, at p. 277.

212. [1943] Que. S.C. 144, at p. 146.

213. SMITH, *supra* n. 112 at pp. 277-278.

214. [1943] Que. S.C. 144, at p. 148.

any *dicta* of Gibsone, J.²¹⁵. When the company was formed, D. was not even a member of it: the lawyers in charge of the incorporation procedures were to remain directors until April 1939²¹⁶, and it is only at that point that D. joined the company. However, the controversy surrounding this question now seems to have been settled definitely by the Court of Appeal's recent decision in *Giguère v. Bourque*²¹⁷. The Court held that the effect of s. 29 is an immediate one: where the company is incorporated, it becomes immediately vested with any contractual right that is held for it by a trustee²¹⁸. In that case, trustees for the future company had entered into a lease with a third party for the benefit of the future company: once incorporated, the company immediately became vested with the rights resulting from the lease²¹⁸ and an action in nullity thereof for fraud had to be taken not by the trustee but by the company which had become, under the terms of that contract, the actual lessee²¹⁹. Similarly, the Court of Appeal held that the company was bound by a promise of sale made to the trustees²²⁰: an action in nullity thereof had to be taken by the company, which was now a party to the contract made in its name. Thus, the Court of Appeal has taken the view that a trust under s. 29 has an immediate effect: it had already suggested in various *dicta*²²¹ such an interpretation that conforms to the wording of the statute.

215. As pointed out above, at p. 41, the case decided that the promoter had to establish clearly his intention to act as a trustee under s. 29. Nowhere does the case report suggest that the company also has to affirm its intention of being bound by the trustee's contract. Smith refers to Gibsone's *dicta* at p. 148 of the report as authority for this: "... There is no evidence that any merchandise was sought to be acquire, or was acquired, by the company; ... The company was unorganized; ... by the letters patent the three incorporators were constituted provisional directors and they were in office, but they had done nothing toward acquiring merchandise for the company; ... 'Surely this is more consistent with the view that Gibsone J., took that D. was owner of the goods and that the company never had an interest therein, having never acquired them. If the learned judge had wanted to give to s. 29 the very peculiar sense given to it by Smith, he would most probably have discussed the point before doing so.

216. [1943] Que. S.C. 144, at pp. 144-145.

217. [1973] Que. C.A. 663. The court, however, refers to no authorities on this point.

218. *Ibid.*, at p. 667, *per curiam*.

219. *Ibid.*

220. *Ibid.* The promise of sale was made to the trustees acting *qua* trustees and also personally. The Court held that in such a case both parties had to sue as plaintiffs: they cannot act "unilatéralement" (p. 667) but must act jointly. In this case, this is a reasonable requirement because both parties are bound by the contract concluded under s. 29.

221. Thus, BROSSARD, J., in *Komery v. Restaurant Komery Inc.* [1965] Que. Q.B. 853 at pp. 856-857 clearly recognized the possibility of binding a company by a pre-incorporation trust. See also: *Morin v. Morin and Provincial Hardwoods Inc.* [1964]

"The company . . . shall *forthwith* become and be vested with all property and rights, moveable and immoveable, held for it up to the date of the letters patent . . ." ²²².

Consequently, it is submitted, a trust created under s. 29 takes effect immediately ²²³ on the issuance of the letters-patent. If the trustee has contracted for the benefit of the future company, it is bound thereby and cannot repudiate the agreement: its recourse would be against the trustee personally if it should suffer any damage as a consequence of any abuse or irregularity ²²⁴.

These views are also consistent with the ordinary principles of civil law. Whenever the Civil Code mentions that a person is seized or vested with property or rights, it makes an important distinction: either that person is vested automatically with the full rights of ownership ²²⁵ or this vesting is qualified. In many cases, the Code indicates that a person is seized of property for certain purposes only ²²⁶ and cannot claim as a consequence the title of owner. S. 29 does not qualify in such manner the company's rights: it "shall *forthwith* become and be vested with all property . . ." ²²⁷. In a sense, the *Companies Act* creates an exception to

Que. Q.B. 854, *per curiam* at pp. 855-856, reversed by the Supreme Court of Canada not on that question but on the issue whether or not in that case there existed a trust: *vide supra*, pp. 41-42. See also: *The T. W. Hand Fireworks Co. v. Baikie* (1911) 39 Que. S.C. 227 at p. 231; A. ROUSSEAU, *Les syndicats ont-ils une âme . . . juridique ?* (1975) 53 C.B.R. 126, at p. 128.

- 222. The French version of the text is even clearer: « La compagnie . . . est immédiatement saisie de toute propriété . . . » If the view taken by the Court of Appeal is right, as a consequence, the company can be the subject of rights and obligations entered into by the trustees before its existence: WEGENAST, *op. cit.*, at p. 262; FORTIN, *supra* n. 113 at p. 89; cf. SOHMER, *supra* n. 149, p. 131 n. 32.
- 223. « La corporation a-t-elle commencé à exister revêtue de cette obligation, absolument comme l'homme vient au monde avec la tache du péché originel ? » in *Les Corporations peuvent-elles être obligées par quasi-contrats ?* (1880) 2 La Thémis 193, 203.
- 224. SMITH et RENAUD, *op. cit.*, vol. I, p. 90 n. 40, have criticized the *Giguère v. Bourque* case, *supra* n. 217, on the ground that if the company is automatically bound it can suffer from abusive contracts or secret profits of the trustees. The weakness of this approach is that the company can sue the trustees if they have failed in their duties towards it rather than be entitled to repudiate contracts that were entered into by a *bona fide* third party. In this respect, the Court of Appeal has indicated that the interests of third parties are to be preferred to those of the company in questions of corporate promotion: *Komery v. Restaurant Komery Inc.* [1965] Que. Q.B. 853, at p. 856.
- 225. See, e.g., articles 607, 795, 891 and 962 C.c. Also: J. S. JAMES, *Stroud's Judicial Dictionary*, vol. 5, 4th ed., Sweet & Maxwell, London, 1974, at p. 2939 n. 8.
- 226. Articles 918, 918 b and 1896 a C.c.
- 227. Thus, it falls in the same category as *supra* n. 225: the right is an absolute one.

the normal rule of civil law trusts²²⁸ but, whatever be the *ratio* of such a rule, it is undeniable that the effect of s. 29 is automatic and binds the company on its coming into existence²²⁹.

If the company is bound on its incorporation by such contracts, is the trustee freed from all liability on the agreements? If one applies the normal rule of civil law, the trustee will not be liable when the company becomes incorporated. Article 981i C.c. reads as follows:

“Trustees are not personally liable to third parties with whom they contract”.

The assumption of liability by the company should, in theory, free the trustee from all responsibility. There is no relevant case on this precise point under s. 29 and the authors do not discuss this issue. However, on the basis of the trust analogy suggested by Rinfret, J., in *Laliberté v. Larue*²³⁰, it is submitted that under s. 29 the trustee should be free from all liability on the company's incorporation.

But what if the company is never incorporated? What if one acts as a trustee for a company that will never come into existence? The question is not an easy one and has not been considered in the context of s. 29. However, a few points are clear. Whether a promoter is liable on a pre-incorporation contract depends ultimately on the other contracting party's state of mind: it is a simple question of intention²³¹. The third party, when he contracts with a trustee under s. 29, always knows that the company is not in existence²³²: as a consequence,

228. Article 981i C.c. shows that the beneficiary under the trust is not seized of the property but must receive a transfer “to vest the property held for the trust in the parties entitled thereto” (981i C.c.). If s. 29 does not mention the necessity of such transfer, then surely it is because of the automatic effect of the provision.

229. The company is in existence from the date of issuance of its letters patent: *Latreille Gaz Naturel Equipement Cie Ltée v. B.C.N. et Lalonde* [1967] Que. Q.B. 259 at p. 261, referring to s. 11 of the *Companies Act*.

230. [1931] S.C.R. 7. *Vide*, generally, *supra*, pp. 361-362.

231. GROSS, *op. cit.*, at p. 199. For an interesting Quebec case: *Hewlings v. Mirotchick*, *supra* n. 177 at p. 27, and authorities cited there; SMITH, *supra* n. 112 at p. 214 n. 13.

232. Because under s. 29 the trustee must contract in trust for a future corporation: see the discussion, *supra*, on the creation of the trust, pp. 363-366.

233. GROSS, *op. cit.*, at p. 186, and more particularly n. 71; also at p. 194 for the rationale of this rule. If indeed the trustee was not responsible, then the contract would have no effect. Thus, the parties are presumed to have wanted a binding agreement, and the only way this is possible is by holding the trustee liable. GROSS, *ibid.* For a similar reasoning, see SMITH, *supra* n. 112 at p. 214 in the general context of promoters' liability in Quebec. See also: *Bonhomme v. Bickerdike* (1900) 17 Que. S.C. 28 (C.R.) at p. 58, *per curiam*. For discussions on breach of warranty of authority in common law jurisdictions, *vide*: L. H. LEIGHT, “Breach of warranty of authority” in *Studies in Canadian business law*, Butterworths, Toronto, 1971, at pp. 359-362 (G.H.L. Frid-

i) if the company is never incorporated, he must have intended to contract with the trustee personally and hold him liable on the agreement²³³;

ii) however, cases clearly indicate that if a trustee explicitly stipulates against personal liability, the third party has no recourse²³⁴. Some authorities suggest however that he could always sue for damages if he can establish that a fraudulent representation was made to the effect that the company would indeed be incorporated²³⁵.

S.29 provides an interesting solution to the question of pre-incorporation contracts as far as binding the company before its incorporation. However, many problems still subsist and the protection of third parties does not seem to be increased in cases of dishonest promoters acting as trustees. The general rights of both the company and third parties will now be examined more closely from the point of view of the trustee's duties in civil law.

4. *The pre-incorporation trust: duties of promoters*

The duties of a trustee under s. 29 cannot be discussed without a more general reference to the duties of promoters in Quebec law. This exercise is not free from difficulties, for promoters' duties in civil law remain to this day a perplexing question. The view is commonly held that there is no jurisprudence in the Province dealing with this important point: one commentator points to "... the complete absence of reported decisions concerning the duty of promoters in Quebec ..."²³⁶. How-

man, ed.); G. SHAPIRA, *Directors without a company and other professing agents* (1975) 3 Otago L.R. 309.

234. The jurisprudence of our courts has always admitted this: *Bonhomme v. Bickerdike* (1900) 17 Que. S.C. 28 (C.R.) at pp. 29, 39-41; *The T. W. Hand Fireworks Co. v. Baikie* (1911) 39 Que. S.C. 227 at pp. 230-232; (1913) 43 Que. S.C. 325 (C.R.) at p. 327; *Hewlings v. Mirotschick*, *supra* n. 177 at pp. 24-25. GROSS, *op. cit.*, at p. 195 for the position of common law provinces. See also: *Canada Business Corporations Act* s. 14 (4); SMITH, *supra* n. 112 at p. 214. As pointed out by GREENSHIELDS, J., in *Lippes v. Tutt* (1926) 41 Que. K.B. 566 at p. 574, "The fact that one person is incapable of contracting and does not contract does not burden another person with that contract . . ." On this last point, see GROSS, *op. cit.*, at p. 198 n. 108.

235. GROSS, *op. cit.*, at p. 194; SMITH, *supra* n. 112 at p. 216. See also: *Irwin v. Lessard* (1889) 17 R.L. 589 (Q.B.) where the respondent purported to act under an authority given to him by the promoters of the future company but this was a false representation: *ibid.*, at p. 593. Liability for damages was also accepted, on this principle, in *Bonhomme v. Bickerdike* (1900) 17 Que. S.C. 28 (C.R.) at pp. 56 and 58.

236. SMITH, *supra*, n. 112 at p. 288; also at p. 212. See the same author, in *Liability of corporate executives for illegal profits in the company law of the Province of Quebec* [1973] R. du B. 253 at p. 265.

ever, the cases do in fact yield a variety of interesting suggestions on this question: whether they deal with the relationship of promoters with the future company or its shareholders, third parties or even *inter se*, they establish a body of rules that can be easily referred to in discussing this issue. This article does not purport to deal exhaustively with the question of promoters' duties in a civil law jurisdiction, but an attempt will be made to enunciate certain general rules whilst examining the problem from the more difficult vantage point of the trustee in Quebec law.

a) Duties of the promoter towards the company

The jurisprudence on this point is rare but interesting. A clear tendency in the case law and the commentaries is to deal with this problem either from the point of view of common law authorities or to adopt a purely civilian approach.

i) Common law

Most cases involving promoters' duties in Quebec have discussed this problem by referring to Anglo-American law. Thus, in *Skelton v. Frigon*²³⁷, the Court of Appeal cites common law precedents exclusively as authorities to be followed on the question of promoters' secret profits in Quebec²³⁸.

Undoubtedly, the most interesting case illustrating this tendency is that of *Larocque v. Beauchemin*²³⁹, a case from the Superior Court of the Province that went on appeal to Privy Council²⁴⁰.

A bankrupt company sold all of its assets, valued at about \$80,000. to the promoters of another company for \$10,000. When the promoters bought this property, they had a clear intention of selling it to the new company and not to buy it for their own purposes; the company was subsequently incorporated and the promoters took up the whole of the

237. (1923) 35 Que. K.B. 11; [1923] 4 D.L.R. 278 (K.B.).

238. *Ibid.*, at p. 11 n. 1. References are made, *inter alia*, to Ehrich, *On Promoters*, *passim*; 20 *Halsbury's Laws of England*, 8 *Corpus Juris Secundum*, various English and American cases, and some decisions of the Supreme Court of Canada on appeal from the common law provinces.

These authorities were considered by the Court in the case in issue but no serious discussion was entered into on their relevance to the problem or to Quebec law generally.

239. (1896) 9 Que. S.C. 73 (C.R.); [1897] A.C. 358 (P.C.).

240. *Ibid.* Note that this case is still considered relevant even in English law: *Halsbury's Laws of England*, vol. 7, 4th ed., Butterworths, London, 1973, at p. 35, par. 47, n. 6.

capital²⁴¹. The company, after incorporation, bought the same properties from the promoters for the sum of \$35,000., part of the purchase price being paid in cash and the balance being credited to the account of the promoters on the shares taken up in the company. When the new company went into liquidation, the liquidator sued the promoters for the payment of their shares, arguing that they had not paid for these shares in the manner required by the Act²⁴² and questioning the legality of the promoters' conduct towards the company. The Superior Court dismissed the liquidator's claim and Jetté, J., in the Court of Review confirmed this judgment²⁴³. On the issue of the promoters' profits, his Lordship said that this sale was valid: it was carried out in good faith²⁴⁴ and the true value of the property was at least \$35,000.²⁴⁵ He then pointed out:

« . . . aucune fraude, aucune simulation ne peut être reprochée aux actionnaires . . . L'arrangement conclu entre eux a été légal, *connu et accepté par tous* . . . »²⁴⁶.

Thus, where promoters hold all of the share capital of a company, the fact that they sell property to the company at a profit does not render this profit an illegal one if every shareholder is aware of the circumstances of this sale. On appeal to the Privy Council, the same position was taken. Lord Macnaghten spoke for the Board:

"Before their Lordships an attempt was made to re-open the charge of fraud . . . It was urged that the price of the property was not fixed or considered by an independent board of directors, and that in this respect the transaction was improper and fraudulent. This argument seems to be based on a misconception of the decision in *Erlanger v. New Sombrero Phosphate Co.* . . . where the facts were very different. In the present case it was not disputed that every single shareholder was perfectly aware of all the circumstances attending the formation of the company, and that nobody was or could have been deceived. Indeed, their Lordships agree with the opinion of Jetté J., who prefaced his judgement by

241. (1896) 9 Que. S.C. 73 (C.R.), *per* Jetté, J., at p. 75. In English law, this is of great consequence: GROSS, *op. cit.*, at p. 127 and following.

242. The case also dealt with the question of adequate payment for shares. In the old statutes, legislation was enacted directing that shares must be paid for in cash. Otherwise, a contract should be deposited with the Secretary of the Province if payment in kind was to be accepted. On this aspect of the case, see the interesting historical analysis in RENAUD et SMITH, *op. cit.*, vol. 2 at pp. 611-613, and more particularly at p. 631 n. 50. Compare with English law, where this is still a requirement under the *Companies Act*, 1948: s. 52 and GOWER, *op. cit.*, at pp. 106-107.

243. Tait, A.C.J., delivered the judgment in the Superior Court.

244. (1896) 9 Que. S.C. 73 (C.R.), at p. 76.

245. *Ibid.*, at pp. 76 and 82.

246. *Ibid.*, at p. 82.

observing that the promoters acted in perfect good faith, and that the value of the property was proved to be \$35,000. at least. »²⁴⁷

A triple test thus emerges from this case: *bona fides*, full disclosure and true value will, as a rule, relieve the promoters of liability for any profit made in a sale to the company. Later jurisprudence however was to abandon the requirement of fair value²⁴⁸ and the rule now seems to be in Quebec, under these authorities, that full disclosure must be made to an independent board of directors, but if the promoters hold all of the share capital of the company, there is no necessity in meeting this requirement²⁴⁹.

Many problems relating to these questions have not received any attention from the provincial courts. However, when one considers that these rules, in common law, are predicated on principles governing fiduciary duties generally²⁵⁰, their application to the law of Quebec can be seriously questioned. The civil law knows of no fiduciary duties: it knows of trustees, mandataries and other representatives but the duties incumbent upon such persons are defined strictly according to the Civil Code²⁵¹. In that sense, the whole of the English law on this point should receive no direct application in our law: as a solution of comparative law, it is of undoubted interest, but the problem of promoters' duties in Quebec should be resolved by application of the principles of the Civil Code governing their relationship to the company.

247. [1897] A.C. 358, in the Privy Council at p. 364, referring to the *Erlanger* case reported at: (1878) 3 A.C. 1218.

248. A curious case is: *A.G. for the Dominion of Canada v. The Standard Trust Company of New York*. A report of the decisions of each tribunal can be found in: [1911-12] Can. Rep. 1 (P.C.). See Also: [1911] A.C. 498 (P.C.). This case was approved in: *Eisenberg v. Bank of Nova Scotia* [1965] S.C.R. 681 at pp. 688-689. The case settled a few questions. Disclosure to the company was taken to mean to all present and future shareholders: *per* Davies, J., in the Supreme Court at p. 17 of the Report; *per* Viscount Haldane in the Privy Council at pp. 39-40. See also GROSS, *op. cit.*, at pp. 98-99. This duty however does not extend to debenture holders: GROSS, *op. cit.*, at p. 109 n. 73 referring to the case under examination. American law takes a wider view of the question: *ibid.*, at pp. 109-111. The case also decided that if all the shareholders have assented to the sale, the relevance of the reasonableness of the price does not arise: *per* Davies, J., in the Supreme Court at p. 21. American law takes a different view of the question: as pointed out by GROSS, "... the burden of proff will still centre on the fairness and reasonableness of the transaction . . .": GROSS, *op. cit.*, at pp. 96, 104.

249. A few cases contain very cryptic *dicta* that seem to be reconcilable only with this proposition: *Chinic v. Canada Steel Co.* (1876) 3 Q.L.R. 1 (C.R.) at pp. 2-3; *Dame Dupaul v. Varyland Investment Co.* (1923) 35 Que. K.B. 328 at p. 332: « Qu'il ait stipulé un profit considérable que lui devait rembourser la compagnie, cela s'est fait ouvertement. . . » (*per* Létourneau, J.). Generally, see GROSS, *op. cit.* at pp. 94-95.

250. GROSS, *op. cit.*, at pp. 79-83, 89 and following.

251. SMITH, *supra* n. 112 at p. 288.

ii) Civil law

It is at this point that a convenient distinction must be made. In Quebec, a promoter might be considered, for the purposes of legal classification, from two angles: he is either acting as a promoter generally or he is specifically acting under a trust established in pursuance to s. 29 of the *Companies Act*. If he is acting as a simple promoter, under what section of the Code should he be considered? The question in our jurisdiction is a novel one and was not considered at all for over a century: however, recent research has suggested that there is authority in the decisions of the provincial courts for considering the promoter as a mere *negotiorum gestor*²⁵². This convenient classification has one undoubted advantage: it allows for the imposition on the promoter of a set of duties and obligations consistent with the economy of civil law. Thus, article 1043 C.c. tells us, *in fine*, that the *gestor* "subjects himself to all the obligations which result from an express mandate". If one then turns to the rules of mandate, one sees that all mandataries are subjected, by law, to a duty to account to their mandator for all secret profits received during the execution of such mandate²⁵³.

A promoter would be bound to account to the company for all profits made during the promotion under these rules: he would, *inter alia*, have to render to the company any secret profit made in pursuance of a sale thereto, unless of course he declares such profit to the company²⁵⁴. The rule, in a sense, would be the same as in English law: being, however, more in accordance with the principles of the Code, it should be preferred to English authorities on this point.

But if the promoter is acting as a trustee, the problem varies slightly. As established previously, trustees under particular statutes in the Province are subjected to the same regimen as the civil law trustee, and as a consequence the rules of articles 981a and following of the Code apply to such persons²⁵⁵. If this is so, they must also render an account of the profits they might have made in any sale to the company in pursuance of their duty to account, specified at article 981 / C.c. No case deals with this point under s. 29 of the Act: however, when one considers the trust analogy established by Rinfred, J., in *Laliberté v. Larue*²⁵⁶, this approach seems

252. SMITH, *ibid.*, at pp. 226-232, 286-289 and 293-295.

253. Article 1713 C.c.

254. *Supra*, pp. 373-375.

255. *Supra*, pp. 361-362.

256. [1931] S.C.R. 7 and *supra*, pp. 361-362.

justified. A duty to account exists in civil law and is required from every trustee, whether he is acting under the Civil code²⁵⁷ or under statute²⁵⁸.

The conclusion on this complicated question is that the problem of imposing duties on promoters in Quebec should be re-examined: whether one approaches the promoter as *gestor* or trustee, the result is the same and in both cases he has to account to the company for monies improperly obtained. The ramifications and variations that spring from this theoretical approach will only be settled by future jurisprudence: it is hoped that the provincial judges will not leave the *terra firma* of civil law when they are next called upon to discuss and settle this question of considerable importance.

iii) The control of the *Securities Act* over the secret profits of promoters

The problem of controlling the profits of promoters in Quebec has taken an interesting turn. In America, promoters' secret profits have now become a point of secondary interest: the strict control exercised over promoters generally by securities legislation has brought about a decline in litigation over such questions. Bruenner and Gilley observe:

"... since the passage of the Act requiring disclosure of promotional profits and interests in the appropriate part of the prospectus, very few cases have arisen seeking the recovery of promoters' profits . . ."²⁵⁹.

The provincial *Securities Act* contains similar regulations. For any person to try to obtain any "gross profit incompatible with the practice of the trade . . ."²⁶⁰ is considered tantamount to fraud. It also imposes on the promoter the obligation of signing a statutory declaration as to the

257. 9811 C.c.; *Racine v. Barry* [1957] S.C.R. 92 at p. 98.

258. It is of interest to note that the other statutory trustee of civil law is under a similar duty to account. Thus, in the recent case of *In re Gérard Nolin Ltée; Bellavance v. B.C.N.* [1974] Que. S.C. 641, it was held that a trustee under the *Special Corporate Powers Act* R.S.Q. 1964 c. 275 had a duty to account and that this duty was to be exercised according to the principles of civil law.

259. *Promoters and their profits* (1958) 13 Bus. Law. 429 at p. 433; GROSS, *op. cit.*, at p. 155 n. 48.

260. R.S.Q. 1964 c. 274 s. 35 (d); RENAUD et SMITH, *op. cit.*, vol. 2 at p. 1193. Is such a fraudulent act to be considered as an ordinary civil law fraud? *Semble*, in common law provinces at least, that the statutory offences cannot be viewed as such. See *Re Attorney General for Ontario and Huteson* (1930-31) 66 O.L.R. 387. Also: WEGENAST, *op. cit.*, at p. 697; Y. CARON, *Aspects du droit des valeurs mobilières*, (1971) 17 McGill L.J. 234, at p. 287.

correctness of the statements contained in the prospectus²⁶¹: this is important because the *Regulations* force the promoter to declare in the prospectus all preliminary expenses²⁶², details concerning the sale to the company of property acquired from the promoters²⁶³, and any payment made to the latter²⁶⁴. Full disclosure of these transactions will usually discourage the promoter from attempting to defraud the Securities Commission or the company, for the civil and criminal sanctions attaching to such violations are severe²⁶⁵. Not content with having set out certain standards in the Act and the *Regulations*, the Legislature also gave the Securities Commission wide powers of discretion in this matter²⁶⁶ and the Commission, in various administrative decisions, has made known to securities issuers generally that it will not grant permission to float an issue if certain safeguards are not met. In relation to promoters, the most important of these are the following:

Bona fides: the Commission must be convinced that the issue is a *bona fide* one and not in the interests of the promoters only²⁶⁷.

Shares in escrow: in order to ensure that the promoters will act honestly, the Commission requires that all shares issued to promoters in consideration of their services or in payment of property sold to the company be escrowed²⁶⁸.

Minimal capital: where the directors have stated that a minimal capital will be necessary for adequate operations²⁶⁹, the Commission insists that an independent trustee be appointed to hold such monies till this requirement is met²⁷⁰. This is certainly a remarkable feature. As seen above, minimal capital requirements in the older *Companies Acts* were

261. *Regulations Made under An Act Respecting Securities* O.C. 2745-73, Que. Reg. 73-417 as amended by O.C. 3963-73, Que. Reg. 73-550 and O.C. 1260-74, Que. Reg. 74-172, at ss. 5(2) and 5(3). [Hereinafter referred to as the *Regulations*.]

262. *Regulations*, s. 5(1)(a); Annex 'A', s. 20.

263. *Ibid.*, Annex 'A', ss. 21, 22, 27 and 28.

264. *Ibid.*, Annex 'A', s. 26. RENAUD et SMITH, *op. cit.*, vol. 2 at pp. 1211-1212.

265. S. 84 of the *Securities Act*. If the promoter's declaration is false, he is liable for damages under article 1053 C.c. for such fraud: *Yuksel Atillasoy v. Crown Trust Co.* [1974] Que. C.A. 442, at pp. 447-448. Also, Martel, *op. cit.*, vol. 2 at p. 356; GOWER, *op. cit.*, at pp. 292, 317 and 320.

266. RENAUD et SMITH, *op. cit.*, vol. 2 at pp. 1188-1189.

267. RENAUD et SMITH, *op. cit.*, vol. 2 at pp. 1192-1193. *Bona fides* was once a requirement set out by the Courts: see *supra*, pp. 374-375.

268. *Ibid.*, at p. 1193.

269. *Regulations*, *supra* n. 261 s. 5(1)(a); Annex 'A' s. 15.

270. RENAUD et SMITH, *op. cit.*, vol. 2 at p. 1194. This requirement applies only in cases where the issue is not taken up wholly by an underwriter: *ibid.* See also at pp. 1212 and 1238.

essentially enacted as a protection against the fraud of promoters²⁷¹. With the advent of modern securities legislation, they disappeared from the statute books²⁷². However, what was once a statutory requirement has now somehow reappeared as an administrative device of some importance²⁷³. The presence of the trustee is also noticeable: trustees for the purposes of holding minimal subscriptions became an anomaly in our law after 1920²⁷⁴ and their reappearance in the administrative requirements set by the Securities Commission indicates the persistent influence of English institutions in this field²⁷⁵.

Options: finally, options granted to promoters are subjected to strict regulation and are generally viewed critically by the Commission²⁷⁶.

The problem of dealing with duties of promoters in Quebec has thus been greatly minimized by the legislative and administrative directives under the *Securities Act*: the active role played by the Securities Commission in this field also highlights the remarkable transition from the tradi-

271. *Supra*, pp. 358-360.

272. *In re Richelieu Oil Co. Ltd.*: J. A. Coulombe et J.A. Coulombe Co. Ltd. [1950] Que. K.B. 714 at p. 722.

273. A clear pattern emerges from this legislative history: statutory protection of investors has now slowly disappeared from the *Companies Act* but the same preoccupations can be found at the administrative level. A good example is the method of payment for shares. In the old Acts, this was rigorously scrutinised: RENAUD et SMITH, *op. cit.* vol. 2 at pp. 611-613. Now this question is dealt with in s. 23 of Annex 'A' attached to the *Regulations* under the *Securities Act*.

274. *Supra*, pp. 357-358.

275. Note RENAUD et SMITH, *op. cit.*, vol. 2 at p. 1194 referring to a decision of the Securities Commission commenting on the « . . . impossibilité dans le droit québécois de créer une fiducie sauf dans des cas spécifiques . . . » (*Farmex Enterprises Inc.*: *ibid.*, p. 1194 n. 356 for the reference). If the Commission recognizes this difficulty, why does it require a trustee in this case? A solution to this problem can be found in French law. Minimal subscriptions must also be held in French law by an independent party: trustees being unknown to French civil law, use is made of a *dépositaire*. See: HÉMARD, TERRÉ et MABILAT, *Sociétés commerciales*, vol. 1, Dalloz, Paris, 1972, at pp. 620-23; ESCARRA et RAULT, *op. cit.*, vol. 1, p. 125 n. 621 where the authors tell us that such requirements were instituted as a protection against the fraud of promoters. See also *Note* (1969) 22 Rev. Trim. Dr. Comm. 1004-05. Thus, in Quebec, if minimal capital requirements are to be utilised again, would it not be more logical to use a *dépositaire* as opposed to a trustee in order to avoid creating unnecessary complications? On deposit, see articles 1794-1812 C.c. It is interesting to note that in the *Proposals for a New Business Corporation Law for Canada*, vol. 2, Information Canada, Ottawa, 1971, par. 15.23(1)(e), the necessity of a pre-incorporation trustee to hold monies pending the incorporation was suggested but was not retained in the final version of the Act.

276. RENAUD et SMITH, *op. cit.*, vol. 2 at pp. 1195-1196. Compare with GROSS, *op. cit.*, at pp. 145-147.

tional protection afforded by the older corporate statutes to a more active supervision of the share markets by an independent body²⁷⁷.

b) Duties of the promoter towards third parties

Apart from the general liability of the promoter on a contractual basis²⁷⁸, most duties of promoters in dealing with third parties are ordinarily discussed in relation with misrepresentations and fraud in the preparation of prospectuses. This question is too complex in itself to be examined in detail in this paper but, for the purpose of the discussion, it might suffice to recall that fraud in civil law is a delict²⁷⁹ and gives rise to liability under the general delictual provision of the Civil Code, article 1053. A promoter dealing fraudulently with a third person will give the latter a personal action in damages for his misrepresentations: in this field, courts have applied common law²⁸⁰ or civil law principles²⁸¹ without much consistency. However, such cases underline clearly that the primary obligation of promoters when dealing with the investing public is one of honesty and good faith²⁸².

c) Duties of promoters *inter se*

Promoters, as a rule, do not necessarily create among themselves any particular relationship: the fact that more than one person acts in the promotion of a company is no indication that such persons have manifested the intention of creating a partnership of promoters²⁸³. However, jurisprudence admits the possibility of creating promotion syndicates and in such cases, participants would be bound towards each other by the ordinary rules of civil law partnership²⁸⁴. There is even some suggestion

277. GROSS, *op. cit.*, at p. 112 n. 86.

278. *Supra*, pp. 371-372.

279. J.L. Baudouin, *Les Obligations*, P.U.M., Montréal, 1970, at p. 83, n. 136.

280. *Bergeron v. La Compagnie de meubles de Jonquière* (1913) 22 Que. K.B. 341 at pp. 349-351 where the Court refers to various authorities of English law and the *locus classicus* on this point: *Derry v. Peek* (1889) 14 A.C. 337.

281. *Bonhomme v. Bickerdike* (1900) 17 Que. S.C. 28 (C.R.).

282. R.R. Pennington, *The Investor and the Law*, Macbibbon & Kee, London, 1968 at pp. 176 and following. See also SMITH et RENAUD, *op. cit.*, vol. 3, at pp. 1428-1437.

283. *Vipond v. Robert* (1908) 17 Que. K.B. 403 at pp. 415-416 *per* Bossé, J.: compare with GROSS, *op. cit.*, at pp. 164-167.

284. MITCHELL, *op. cit.*, at pp. 19-20, 254-255. *Hopper v. Hocror* (1905) 35 S.C.R. 645; *Komery v. Restaurant Komery Inc.* [1965] Que. Q.B. 853 at p. 857. See also the *Companies Information Act* R.S.Q. 1964 c. 273 s. 3 where the possibility of creating such a partnership seems admitted. Some of our courts have taken the unusual view

in the cases that pre-incorporation trustees might also enter into some form of *société*²⁸⁵ and be bound by the same rules²⁸⁶. Parties might also wish to prepare a pre-incorporation voting agreement and in such a case, their relationship would be governed by the ordinary rules of contract²⁸⁷.

In Quebec law, the promoter, whether he be considered as a *gestor* or a trustee under section 29 of the *Companies Act* is thus bound by a clear set of duties that is remarkably similar in substance to those imposed on promoters in common law jurisdictions. However, the interest of such an analysis is not to create confusion for the pleasure of uncertainty but to indicate that in a civil law jurisdiction it is inevitable that corporate promotions will be regulated by principles peculiar to the economy of civil law and that uncritical references to common law precedents brings about much more obscurity on such points than the contrary exercise.

Conclusion

From the historical perspective, one can draw interesting conclusions. The existence of unincorporated companies in Quebec as early as the late eighteenth century²⁸⁸ is proof that English law had considerable influence in the field of corporate activities even before the enactment in 1868 of a *Companies Act* modelled on the English statute²⁸⁹. However, that influence had clear limits: as seen above, the provincial courts and legislature soon intervened and indicated that such companies in Quebec were nothing more than ordinary partnerships familiar to civil law. In a sense, by assimilating the unincorporated company to a mere *société*, jurists in the Province demonstrated their determination to preserve the purity of the civil law heritage.

that the pre-incorporation partnership is sometimes continued in the new company: *The Windsor Hotel Co. v. Date* (1881) 27 L.C.J. 7 (S.C.) at p. 10 and a similar view is sometimes accepted in America: GROSS, *op. cit.* p. 172 n. 7. This view, as far as Quebec law is concerned, has been severely criticized and is not followed. *Vide* Smith, *supra* n. 112 at pp. 230-232.

285. Brossard, J., in the *Komery* case, *ibid.*, said at p. 857: « Les actes posés par les membres de la société *sui generis* constituée pour fins d'incorporation ne peuvent, sous les réserves sousdites quant au fidéicommis, lier, *in futurum*, une compagnie non encore formée . . . ».

286. Articles 1839 and following C.c.

287. A good example is to be found in *Latreille Gaz Naturel Equipement Co. Ltd. v. B.C.N.* [1967] Que. Q.B. 259 at pp. 259-260. *Vide* also the Supreme Court of Canada decision in: *Tannenbaum v. Sears & S. Sears Real Estate Ltd.* [1972] S.C.R. 67 (Ont.) and a comment on that case: SOHMER, *supra* n. 149 at pp. 128-130.

288. *Supra*, p. 347.

289. *Larocque v. Beauchemin* (1896) 9 Que. S.C. 73 (C.R.), at p. 76.

The discussion on unincorporated companies introduced an examination of the problems created by the pre-incorporation trust in Quebec. Notwithstanding its obscure origins²⁹⁰, the pre-incorporation trust soon became a valuable promotional device and one notices, in recent years, a proliferation of cases dealing with this issue. Two remarkable features can be observed in this discussion. Firstly, a similar process of assimilation is apparent in this case as in the case of the unincorporated company: serious authorities suggest that the trust created under s. 29 of the *Companies Act* must be understood according to the rules of civil law trusts and not those of common law. Thus, when one studies the reactions of the provincial judiciary to the pre-incorporation trust and the unincorporated body, one finds in both instances a tendency of trying to assimilate common law inspired institutions to the rules of civil law.

The second point of interest in the discussion under s. 29 of the Act is that it highlights a clear transition in the legislative techniques utilised to protect investors. The earlier corporate statutes offered numerous safeguards against the fraud of promoters and a good example of this preoccupation was the minimal capital requirement. This legislative approach has been abandoned over the years in favour of the more flexible control afforded by the *Securities Act*. The control of promotional irregularities is best carried out by an *ad hoc* investigation on the part of the Securities Commission as opposed to the rather rigid statutory safeguards that are more easily avoided. Finally, it becomes increasingly clear that, whether the problems of investor protection in Quebec are approached from the viewpoint of the *Companies Act* or the *Securities Act*, the inescapable conclusion is that the incidence of civil law on such questions cannot be avoided and must be considered in its many implications.

290. *Supra*, p. 354. The pre-incorporation trust was thus a creature of jurisprudence: perhaps an application of the maxim "communis error facit jus" is apposite in this case. See H. BROOM, *A selection of legal maxims*, 10th ed., Sweet and Maxwell, London, 1939, at pp. 86-87.